Credit and Capital Formation

a report to the President's Interagency Task Force on

Women Business Owners

The Treasury Department Study Team

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PREFACE

The Interagency Task Force on Women Business Owners was established by President Jimmy Carter on August 4, 1977. The Task Force was given a four-fold mandate:

1. To identify primary practices or conditions which discourage women from becoming entrepreneurs or which have the effect of discriminating against women entrepreneurs or place them at a competitive disadvantage in the marketplace;

2. To identify and appraise existing data, the adequacy of information and the methods for collecting additional data;

3. To assess Federal programs and practices that may adversely affect the initiatives of women business owners or may discriminate against them or which mitigate discriminatory practices and conditions; and

4. Based on their findings to propose changes in Federal laws, regulations, and practices and to advise on the budgetary impact of these proposals.

The Task Force efforts concentrated on small business because the majority of women-owned businesses are small businesses. The Treasury Department Study Team was made responsible for the section of the report on credit and capital formation as well as other financially related issues such as insurance, bonding, and taxation.

Other major areas of the Task Force effort and the agencies responsible for developing sections of the final report were:

-- Education and Management Training -- Department of Health, Education and Welfare;

-- Marketing and Procurement -- Department of Defense and General Services Administration;

-- Legislation and Regulation Problems -- Federal Trade Commission;

-- Assessment of Overall Data on Women Business Owners -- Department of Labor;

-- Assessment of Federal Programs Currently or Potentially Impacting Women Business Owners -- Small Business Administration; and

-- The Department of Commerce chaired the Task Force.

Central to the issue of credit and capital formation was the role first of the private sector, mainly commercial banks, and, to a lesser extent, finance companies and venture capital firms; and second the role of the public sector, particularly the various loan programs of the Small Business Administration and the thrust of the Office of Minority Business Enterprise (OMBE), Department of Commerce. The Study Team found that not one law, regulation, or program specifically and explicitly assists women business owners.

Another vital issue was that of taxation. Since tax laws are sex neutral, the Study Team presented those key tax provisions impacting upon small business and recommended support of the Carter Administration proposals relating to small business. In addition, we recommended a new jobs employment credit and simpler forms for payroll taxes and retirement plans.

Finally, the Equal Credit Opportunity Act (ECOA) and Regulation B, which enforces the Act, were analyzed and evaluated and, in conjunction with a thorough analysis by the Federal Trade Commission, recommendations were made by the Study Team to make several changes in Regulation B so that it will protect women business owners seeking commercial credit.

Although this study concentrates on the barriers to women business owners and the needs of women business owners, we hope it will have a broader use. We believe our study is the first government survey which presents so many aspects of credit and capital formation as it relates to small business.

ACKNOWLEDGEMENTS

This study is the product of the efforts of a great many people brought together to try to accomplish a herculean task in an impossibly short period of time. The core of the Study Team was made up of Jean LaForce from the private sector, Abby Gilbert from the Office of Economic Policy--Treasury Department, and Rosemary Lynch from the Export-Import Bank. Other direct contributions to the report came from Margaret Fowler, Alison Ruml, and Ron Torrence. Research assistance was provided by three of my students from the American University, Ferris Brown, Brenda Barbuto, and Larry Manley. Carol Oman, a banker from the private sector, coordinated our efforts with the rest of the Task Force and also gave us valuable advice and assistance. A great debt is owed to Lois Holland and Janet Paluck, our secretaries, for the tireless and efficient assistance they rendered throughout the study and report writing. Hattie Dorman of the Internal Revenue Service and her roundtable of minority women entrepreneurs provided us with valuable insights.

Several hundred persons were interviewed in person and by telephone during the course of the study, some several times. I thank them all for the valuable information. Also, I would like to express appreciation to my advisors on the study, Patricia M. Harvey, Deputy Assistant Secretary (Administration) of the Treasury, and J. Elton Greenlee, Director of the Office of Management and Organization, who so graciously arranged interviews with former top policy-makers of the Department and gave such good advice.

This has been a collaboration in the fullest sense of the word. All of us who worked on the project contributed much and, I'm sure, learned a great deal.

I hope our excitement and some measure of our new knowledge and understanding is conveyed to the readers of our report.

Theodora K. Watts
Study Director

Washington, D.C.
June 1978

1 INTRODUCTION

The basic assumption underlying the Credit and Capital Formation Study was that obtaining sufficient funds to start or run a business is a major problem for women business owners. This is not to say that men do not experience the same obstacles, nor that women's problems are a direct manifestation of overt discrimination. We assumed that women entrepreneurs suffer from the same shortcomings as all small business owners; that is, lack of management experience, marketing expertise, financial planning ability, and knowledge of the money and banking systems in the United States.

The study effort was designed to meet two rather different needs. First, the report contains information needed by the Task Force to formulate policy recommendations related to women in business. Second, we hope the report provides information needed by women who have or are interested in owning businesses. In our data gathering we attempted to restrict ourselves to the financial aspects of the woman-owned business, primarily capital formation and credit, and, secondarily, other financially related operational areas such as accounting, insurance, bonding, financial planning, cash flow management, and taxation.

In attempting to assess problems women entrepreneurs might have in obtaining credit and in capital formation, a two-pronged approach to data gathering was designed. The first gathered information from women business owners, or potential owners, themselves. This was done primarily through the Task Force questionnaire which was mailed out to 30,000 individuals.(1) Additional input was gleaned from roundtable discussions held in six major U.S. cities with banking and entrepreneurial participants, both men and women. These roundtables brought together officers from banks who are involved in making small business loans or who have some knowledge of women who apply for loans, and women business owners, themselves.

In addition, a series of interviews was conducted with banking officials in the same cities as the roundtables: Atlanta, Chicago, Dallas, Los Angeles, New York, and Washington, D.C. These officers were policy-level persons in charge of commercial lending or with a direct knowledge of commercial loan policies and practices, as well as individual commercial loan officers. All these were structured interviews designed to obtain such basic information as: how women business owners or potential owners are being perceived by the banks; what factors influence loan officers' decisions; and the level of commercial loan activity the banks are engaged in with respect to small business in general.

We found that loan decisions are made on the basis of:

-- Relative risk of nonrepayment. Banks loan their depositors' money. They do not make high-risk loans. Small businesses are by nature high-risk for a variety of reasons. Relative credit-worthiness of the individual applicant is another measure of risk.

-- Relative return on the money. One large loan costs far less to administer than many smaller loans. Loans under $50,000 are not cost beneficial to administer for many banks, especially the larger ones.

-- Availability of bank funds. Is their money available to make this type of small business loan, or are the funds better used elsewhere (e.g., loans to larger corporations)? In tight money situations, existing customers are serviced first.

The second phase of the data gathering was an assessment of the investment climate in the United States, including business and economic trends for the past three years. On this basis we offer a tactical economic investment outlook. By definition, a strategic economic assessment is not within the scope or capacity of this study.

Specifically, this phase of the study is composed of interviews with venture capital/investment banking firms, including small business investment companies, brokerage houses, commercial firms, and insurance and surety bonding companies. Within each of these areas, interviews, both in person and by telephone, were conducted after research and analysis of published materials. The trade associations were also interviewed for data which they had generated on women and credit.

An in-depth literature search and contact with the Federal Reserve System for books, journal articles, reports and data completed the information gathering for this section of the report.

The study is divided into four parts discussing financial aspects of pre-entry to business ownership and actual market entry; capital formation; credit; and taxation issues. Each of the sections will discuss the financial needs and requirements of women business owners, barriers to meeting these needs, existing programs and legislation, and recommendations for action. The barrier discussions include an assessment of existing data and results of surveys conducted by, or in conjunction with, the Task Force.

Initially, much of the information gathered in the interviews, the roundtables, and the Task Force questionnaire seemed to be contradictory. On the one hand, we heard horror stories of the difficulties women were having obtaining credit and building capital. On the other hand, some women entrepreneurs and financial officers were saying that women are not treated significantly different from men -- the only qualification being that women had to work harder and be tougher because they received so little support from society, that is, they are not allowed the luxury of mediocrity.

One banker, toward the very end of the data gathering exercise, put his finger on what we had been hearing. He said he had found that women seeking commercial credit fall into one of two general groups. The one group seems to be interested in going into business as an outlet for the individual. These women are looking for a way to make their hobbies pay off. They often want to work out of their homes with their "business" more a sideline. Most often they plan to do some kind of small-scale retail selling or offer a service such as child-care or catering. Seldom would the loan requested be more than $10,000 for the home-based activity or $25,000 for the boutique-type of operation.

The other group of women is interested in a true entrepreneurial venture. Their ideas concern more substantive activities such as manufacturing a hard product or selling a professional, usually high technology, service. Such activities would have the potential, at least, of producing a more meaningful overall impact in an economic sense, such as creating more jobs or paying taxes. The banker's question was, should the Government be involved in facilitating entry into business ownership for the first group?

Within this second group of women are two major subgroups. The established business owner and the potential business owner. (The first group is, by and large, made up of potential business owners.) We found that the problems of these two subgroups are quite different and our report attempts to deal with issues that are important to both.

In analyzing the written materials and the data collected in our field study we can state only that our findings are inconclusive. We found little or no direct evidence that women have unique problems in obtaining business credit <u>all other things being equal</u>.

We found what appears to be what might be termed an entrepreneurial sequence operating. A person obtains training of some kind, works in a position for a number of years, then makes the decision that he or she wants to own the business. Not all people are willing to take the risk or put in the work effort that business ownership requires. Women are now entering this pipeline in increasing numbers. They have invaded the corporate hierarchy, but relatively few seem to be ready (or willing) to take that risk at this point in time. There is, however, a high degree of agreement among the people we talked to that there will be major changes in the patterns we now see over the next ten years. The numbers of women interested in business ownership are increasing dramatically.

2 MARKET ENTRY

In recent years the expectations of many women regarding their place in society have changed rapidly and dramatically.(2) But one expectation that has not changed among women is the belief that they cannot or should not become businesswomen. Economic independence for women is seldom expressed in terms of entrepreneurship. The American dream that a person can start a small firm and by hard work see it grow into a large business is part of only a very few women's dreams. Women have had a negative perception of business and making profits.(3) The question we will explore in this section of our paper is whether socialization has affected woman's image of herself, her educational choices and her occupational path to such an extent that her ability to obtain the capital and credit necessary to begin her own business is hampered.

Socialization

Women are brought up with exposure to very limited role models; there have been few highly successful women in the business world. This is one of the greatest barriers to their becoming businesswomen. Very few women are able to visualize themselves as entrepreneurs. Women have been taught to be dependent and to be "feminine;" thus, the values and varieties of behavior among women are shaped and modeled by their situation within society. Psychologically female financial ambition and the need for economic self-sufficiency is at odds with the role learning and role acceptance which begins almost at birth. Traditionally women have been socialized to achieve in directions other than owning and managing their own businesses. Society still seems to believe that women are not as serious as men about handling financial and business matters.

Socialization thus has left an impact on woman's conception of herself as a potential businesswoman, and shaped her educational and occupational choices.

Education

In part due to socialization, women have not, in the past, pursued educational choices that would lead to the higher earning jobs in business and management. This decision can become extremely important at a later time, for with higher earnings a woman would have greater savings and a larger equity base from which to borrow additional funds to form a business. Until very recently women's own socialized inclinations were reinforced by real sex bias in the educational opportunities open to them and the degree to which they were steered away from traditionally "masculine" fields.

Understanding the impact of socialization on income is important. Level of education is directly related to the level of work force participation; better education means better jobs, e.g., women with college degrees are more likely to hold managerial and professional jobs than women without college degrees. But there has been a reluctance on the part of women entering college to seek a business degree. Prompted by a family environment into an assumed "proper female role" of passivity, and reinforced by educational and counseling experiences, women tend to exclude preparation for the business world. They stay, consequently, a step behind men and are ill-prepared to parallel the advances made by their male counterparts in the economy. They are not as knowledgeable as men about the financial and banking systems, especially how to obtain business credit and how to establish a good credit history, and, perhaps even more important, they have no knowledge of or experience with the financial community. Women also lack vital empirical knowledge of how the business world operates.(4)

More and more women are obtaining college degrees, but a large number of these women lack professional preparation in the field of business. Until very recently statistics and research show that few women entered what are considered either masculine fields or nontraditional subject areas; namely, mathematics, economics, finance, and business. Most women have not been sufficiently prepared in high school to take these courses. They then do not feel ready to pursue such courses in college; and those women who do, do not take enough courses to prepare them for occupations in the business world which are related to these fields. Though girls will begin in first grade with better marks in arithmetic than boys, and in all of elementary school boys and girls seem to like math equally well, somewhere along the line girls apparently lose interest and demonstrate less proficiency. This situation becomes more serious as allied business fields of economics, finance, and accounting become increasingly quantitative and analytical.(5)

In one famous study of women who had achieved high-level managerial positions, many of the women in the sample who attended college in the 1930s took nontraditional or male oriented courses, but only one-quarter of this group took business and economics and under ten percent chose math.(6) In 1976, a similar survey showed only a slight increase, with 32.5 percent of all women receiving degrees in nontraditional fields; 6.7 percent took degrees in business and management; and mathematics declined to 1.5 percent.

At the graduate level there is evidence that more women are now beginning to chose the kind of education that has helped pave the way for men in business. This is significant, since education beyond the undergraduate degree appears to be the most important factor in the employment status of women and attainment of the managerial level of responsibility. The percentage enrollment in graduate schools of business is rising; the number of women taking the admissions tests to these schools has risen from 3.3 percent in 1966-67 academic year to 8.0 percent in the 1971-1972 academic year. Between 1972 and 1973 women enrolled at Harvard Business School, which did not admit women to its MBA program until 1963, rose from four percent to seven percent in one year. And at Columbia University's Graduate School of Business, which has always been open to women, enrollment jumped from five percent in 1968 to 21 percent in 1973; while Stanford's Business School saw enrollment skyrocket from 1.6 percent in 1970 to 18 percent four years later.

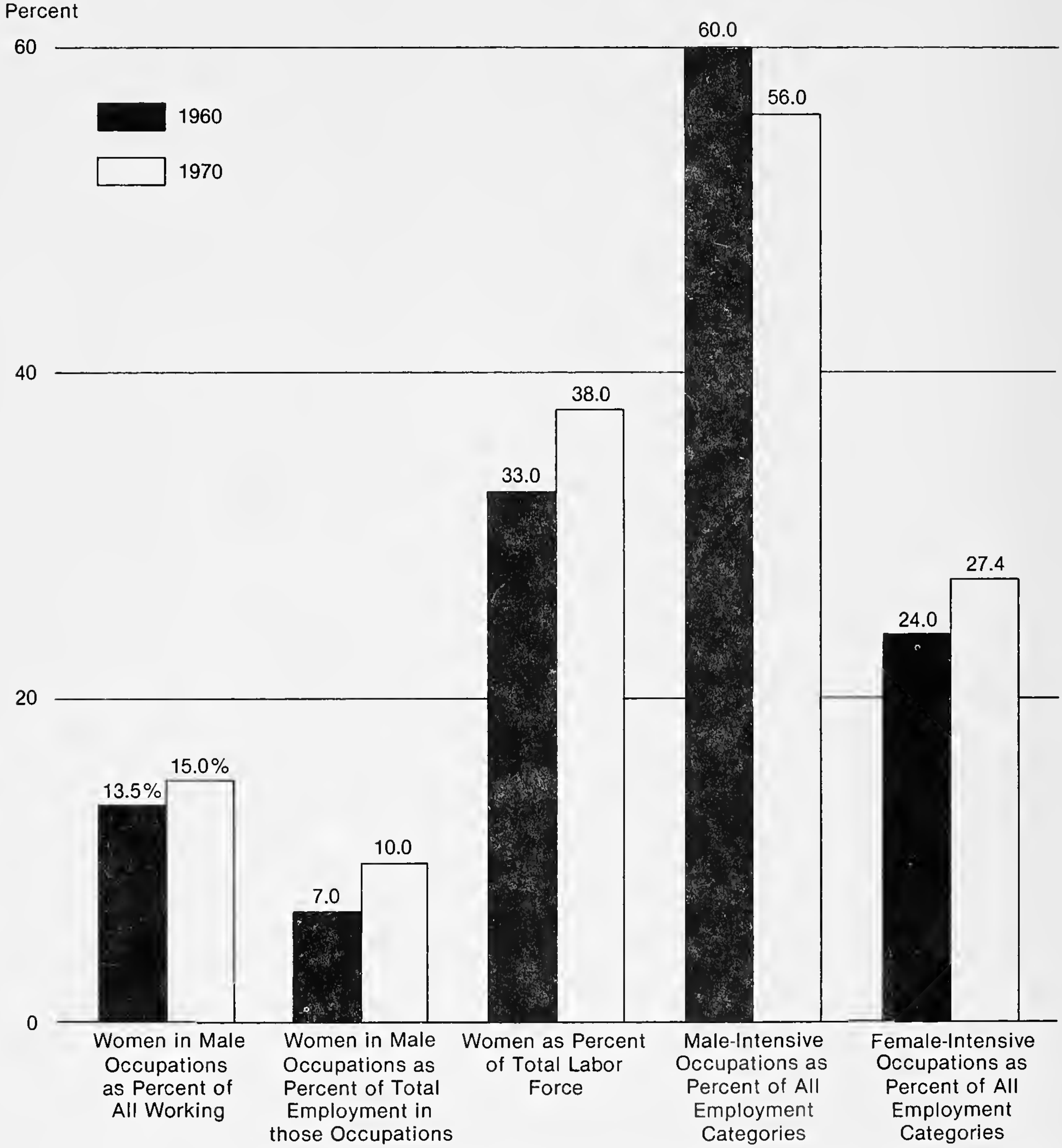
In summary, female enrollment in prestigious business schools has shot up dramatically. Unfortunately, this does not tell the whole story, for women graduating from these programs are trained to fit into a corporate environment, not to own their own businesses; these courses of study are often found to be of little help to the entrepreneur.(7)

Work Choice

Socialization and sex stereotyping have affected the quality of women's work experiences. Such discrimination has repercussions for women-owned businesses in two ways: (1)

CHART 1

Representation of Women in Male-Intensive Occupations



SOURCES: Reubens and Reubens, *American Women Workers in a Full Employment Economy, A Compendium of Papers,* Joint Economic Committee, 1977, p. 108.

Bergmann and Adelman, *The American Economic Review,* LXIII (September 1963), 511.

the types of businesses women own, and (2) the capital needs of those businesses. The occupational concentration and job segregation of women into traditional "female" jobs closely parallels the concentration of women-owned businesses in services and small retail establishments. This has contributed to the low earnings of women in the job market, and having lower earnings reduces women's ability to build sizeable personal savings. Lack of sufficient personal savings restricts, if it does not prohibit, women from acquiring pools of capital on which they can leverage additional funds. Low income is thus a barrier to business ownership.

The persistence of occupational segregation by sex in the labor market is the major obstacle to the attainment of economic equality for women. Occupational segregation by sex appears to be as pervasive now as it was years ago. The occupational distribution and status and pay of women within each occupation has not changed significantly since 1940. While women have gained much more access to market employment they have not gained full equality in the choice of jobs and opportunity for advancement. Women still remain in traditional sectors and female jobs such as clerical-sales, professional-technical, and operatives.(8) In 1977, 34.7 percent of all women workers were in clerical jobs compared with six percent of all men; 1.6 percent were in crafts and 11.8 percent in operative jobs compared with 21 percent and 18 percent, respectively , for men; and one in every 20 women was in a managerial or administrative occupation compared with one in every seven men.(9)

Are women moving into nontraditional, male-dominated occupational fields, and, if so, what are the implications for women-owned businesses and for women's earnings? Traditional and nontraditional jobs which women hold are not a fixed category but vary over time and industry. A traditional job is defined as one where women appear in considerably larger proportion than their incidence in the total work force. A nontraditional job has the opposite characteristics.(10) Chart 1 shows that the proportion of women in male-intensive jobs has changed little; however, during the 1960s there was a very small increase of women entering traditionally male-dominated jobs, such as skilled trades and the professions and managerial positions.

Women are beginning to move into management positions, many are now at the middle level. This step is important since one major barrier to business ownership among women is their lack of experience in management. These management jobs will give women knowledge about business practices and experience and exposure to the available sources of credit and financing. Management jobs will give many women the same experience as men, experience which weighs heavily in the granting of credit. More important, it has been suggested that as more women move into management, they are more likely to assume the risks of entrepreneurship.(11)

Women are not only heavily concentrated in a few occupational categories, they are at a lower level of all categories of employment and they have little vertical mobility and opportunity to move into the top levels of a given occupation. Discrimination against women in male-dominated occupations,(12) concentration in a few "female" occupations, and relegation to the lower ranks of all occupations have been the major reasons for the enormous pay differential between men and women. Women earned 57 percent of what men earned in 1974, compared to 64 percent in 1955. Low earnings are the greatest single barrier that women have in building up their own capital and obtaining bank credit.(13)

Recent research has shown that there is a lessening of the pay differential.(14) When occupation groups and other job factors are sufficiently disaggregated and changing social attitudes are taken into account, the long-run prospects for women's earnings are favorable. Other studies have shown that women who moved from female- to male-intensive jobs made the largest percentage gains in hourly wage rates.(15)

Women and Wealth

There is a persistent myth in America; many people believe that women control the nation's wealth. There is some truth to this statement, women own almost half of the nation's wealth -- 47 percent in 1975.(16) Their ownership of common stock has fluctuated from over half of all shares in 1965 to slightly less than half in 1975.(17) Most women who become wealthy do so through inheritance from their fathers or husbands. These women are usually in their sixties, 54 percent of them are over 65 years old. Rarely does any woman achieve affluence on her own.(18) But there is a great difference between ownership and control of wealth.

Women control very few economic decisions.(19) The wealth women inherit is controlled and managed by large banks and trust companies, by large corporations, by accounting and legal firms, and by governments issuing bonds -- all organizations where women have little ability to control decisions.

For example, individually held shares in corporations do not enable women to influence business policies because the shares are too widely distributed and women shareholders have shown neither the inclination nor the ability to organize in order to collectively influence corporate decisions. Women do not control wealth as investors; they do not control their money; and they rarely make decisions on the buying, selling or trading of the stocks and bonds they own.(20)

Women's ownership of securities has implications that could have an impact on the American economy if women begin to exert control of their wealth; for women have been shown to be more conservative investors than men. They look for safety and security and feel safer with blue-chip stocks, bank time certificates of deposit, and corporate bonds. Women strongly prefer companies making consumer products, especially goods they themselves use, and avoid heavy industry issues.(21) As more and more women-owned wealth is controlled by conservative trust officers and banks, and the female penchant for investments in bonds, high grade stocks, and cash reserves is thus fortified, the percentage of wealth available for high-risk venture capital shrinks.(22) No evidence could be found by the Study Team of the investment of women-owned wealth in businesses owned by other women, e.g., through mechanisms such as capital pools for investment.

Entrepreneurship

Women have not developed a sense of their own potential as entrepreneurs; their aspirations are too low. From our colonial times, women have owned businesses but the woman-owned business has always been small.(23) Some have termed women-owned businesses "micro-enterprises." A very few but significant sociological studies have looked at the female entrepreneur. Their results indicate that women have the same entrepreneurial personality characteristics -- risk-taking, independence, high achievement -- as men.(24) Thus, a tentative conclusion may be drawn that it is the socialization process that limits a woman's view of herself as an entrepreneur.

What is an entrepreneur? An individual who builds a business that did not exist, who stands to gain significant financial rewards or suffer large financial losses, and who has operational freedom and decides upon alternatives is an entrepreneur. An entrepreneur and a manager are usually not the same person. Though hard work and dedication may be common characteristics, the drive to succeed in one area does not necessarily mean that the drive will bring success in the other.

What are the personality characteristics of an entrepreneur? One major motivation of an entrepreneur may be the desire to be independent and to achieve. He or she often also possesses energy, competitiveness, and, perhaps most important, are self-disciplined, persistent, assertive, confident, determined and decisive. They are action-oriented as well as goal-oriented, and they are optimistic -- they have a positive attitude about the future. To conclude, the limited studies that have been done have shown that there is little difference between personality characteristics of male and female entrepreneurs. In those areas where there is a small difference, it is not attributable to personality characteristics but to historical development.(25)

The crucial factor of willingness to take risks is similar in both male and female entrepreneurs, and entrepreneurs are rated as moderate to high risk takers. Entrepreneurs do not seem to see failure as a real possibility. However, men and women perceive risk differently. Thus, while male and female entrepreneurs may have the same risk-taking characteristics, the perception of risk seems to determine whether an individual will become an entrepreneur. Men see risk as either positive or negative, loss or gain, danger or opportunity. Women see risk only as negative. Men see risk as affecting the future; women see risk as impacting upon the present. It appears there is a difference in response because of a difference in perception, and a difference in behavior as a consequence of both. Most women appear to have seen the risks of business ownership as being too costly to attempt to surmount the barriers to success.(26)

Women entrepreneurs and managers have been found to be different from other women. Early on they worked hard, set goals, established priorities, and rejected women's traditional social goals. Female entrepreneurs were found in one study to be special people: they worked, achieved, fought for their judgments, and sacrificed private time and emotional energy. They also had a high sense of self-worth; they never felt they could not do something just because they were women. Being a businesswoman did not seem to affect their perception of themselves as women; they maintained strong feelings about that role and only a minority felt they sacrificed their femininity in order to establish their businesses.(27)

The Credit and Capital Formation Study Team found considerable evidence in their field study to support these viewpoints from the literature, and these will be discussed throughout the remainder of this report.

Starting a Business

A woman must have three things before she can start a business:

(1) She must have a marketable idea.
(2) She must have management ability.
(3) And she must have the funds needed to finance her business for at a least a year.

These same requirements are imposed on all small business owners; women, however, have not generally shown an understanding of what these requirements mean. For example, one must have a marketable idea. Women business owners have traditionally been clustered in small retail selling, the boutique is most often cited, and in supplying services. Paradoxically, these types of businesses have the lowest return on investment and the highest failure rates.

Management ability is the second prerequisite. Our research shows that education and work experience are used by lending institutions as indicators of sufficient management skill. Women have not until recently pursued careers or academic degrees in management.

Because of the inadequacies in the first two requirements, women have a problem with the third. The broad concept of financing a business incorporates both the knowledge of how to raise capital and acquire credit and knowledge and experience in financial management.

Simply stated, the financial needs of a business are capital and credit. These two terms convey two entirely different concepts which should not be confused. Capital are those monies (or other tangible assets) invested in the firm by the owner(s) for use in conducting the business; capital cannot be withdrawn except through dissolution of the existing business entity. Credit, on the other hand, is the ability to obtain goods, services, or money in exchange for a promise to pay in the future. For the small business, credit usually takes the form of either short-term financing from banks (or finance companies) or trade credit. Thus, sources of funds, aside from family or friends, are commercial banks, commercial finance companies, venture capital firms, and, to a very limited extent, savings and loan associations and credit unions.

Many fledging entrepreneurs operate under the misconception that the primary function of a commercial bank is to loan money. This is not so. Because so many new businesses fail, banks do not usually lend money to start a business, except for small, often installment payment loans (up to $15,000), which must be personally secured by the borrower. The primary function of a commercial bank is to provide a return on investment to the bank's shareholders. The mechanism by which the bank provides this return is through charging for its services, such as making loans and charging interest. Commercial banking lending practices to new businesses will be addressed in a separate section of this study.

Like banks, finance companies bridge short-term financial needs. However, finance companies will lend to riskier proposals and accordingly charge significantly more in interest fees than the commercial bank.

Venture capital firms make long-term equity (or capital) investments in businesses. These firms appear to play a very small role in the financing of new or existing women-owned businesses. Venture capital firms finance companies through any one of five stages of development (start-up, first through third stage financing, bridge financing and buy-out, or acquisition, financing). The Study Team surveyed venture capital firms for their experiences with women-owned businesses, the results of which are addressed later in this report.

Loans from savings and loan associations for commercial purposes (other than refinancing one's house to pull equity out for reinvestment elsewhere) are limited to certain real estate and/or construction applications. Also authorized are loans secured by savings deposits or certificates at the association of an equal or greater amount. These share loans are also available at credit unions. They can be used to raise business capital, while permitting investors to earn interest on their existing savings.(28)

Thus, in addition to the entrepreneur's idea for a product or service, many other factors must be considered if this "idea" is to come to fruition.

Financial Planning

What are the barriers which women encounter in market entry? Whatever avenue of approach an entrepreneur takes, whether she perceives a need for a product or service which she feels she can provide or simply wants the pleasure of expanding her hobby into a small boutique, the objective must necessarily be to make a profit. Yet thousands of new businesses fail every year due to poor management and lack of adequate financing. The basic requirements of a successful start up in business are frequently the very ones which women still lack. These are: basic financial planning, managerial expertise, and access to sufficient capital and credit. Managerial expertise and full access to capital and credit markets are discussed elsewhere in this paper; let us examine here basic financial planning and loan applications.

Market entry necessarily assumes a small firm with all the concomitant riskiness inherent in small business finance. This financial risk falls into three main areas. First, many capital markets are not available to small firms simply because of diseconomies of scale. Hence, small new firms must rely to a greater extent on internally generated funds. (This point is addressed in the section of the report entitled "Availability of Capital.") Second, working capital management is of vital importance. Funds are generally very limited, trade credit is expensive and rapid expansion of scale can lead to a cash flow crisis and insolvency instead of the rising net income the business owner expected. Third, because the business is generally trying to establish a niche for itself in an already on-going industry, it must have financial management which is not only competitive with but superior to that of other market participants -- it cannot permit itself to fall below industry standards and expect to survive.

As noted in Dun's Review, "a great number of companies have managed to overcome the handicaps of size and operate successfully among the giants. Most of them have one thing in common: a carefully planned strategy."(29)

The Business Plan: Few women business owners who were contacted by the Study Team had ever made the first essential step in successful market entry, that is, a detailed business plan. By this we mean beginning with an analysis of what business the firm is in and continuing on to encompass all aspects of strategic planning by relating objectives, goals, and resources, both financial and personal, to the environment. The following is a list of business plan components which should be included:

-- description of the business(30)
-- anticipated market
-- competition
-- location of the business

- management resources
- personnel resources
- how credit will be used and the expected effect of any loans
- summary

If the small business is going to be engaged in more than one activity, the central activity should be defined and committed to paper. All too many businesses have ended in bankruptcy proceedings because of confusion as to the main purpose of existence and the diversion of funds to a secondary endeavor. The entrepreneur's entire planning effort must be based on her perception of the specific business she wants to be in.

Developing a business plan is not easy. It requires management time, and it requires the use of financial techniques which may be unfamiliar to many entrepreneurs. The return is great for those who can develop sound financial plans, however, as such planning greatly extends the entrepreneur's control over her business. The marketing and financial analyses are instrumental in determining the amount and type of financing which is needed, and the planning framework leads to a long-term program of financing, including helping to build a good "teamwork" relationship with a bank. According to the bankers we interviewed, incomplete or ineffective financial management is the major flaw in a large percentage of otherwise well-run small businesses in the country today.

Professional assistance in developing business plans can be very helpful, but caution should be used in the selection of someone to help. There are many who can talk good finance, but who cannot deliver it. The company's accountant is a good place to start, however, many accountants have neither the training nor the inclination for financial planning work. The company's banker may be helpful, as some banks have management assistance programs, and in other cases a good loan officer can refer the business owner to a professional consultant in financial management. Other sources of help are the Small Business Administration and the Office of Minority Business Enterprise in the Commerce Department. Local colleges may also offer management consultation through their business administration faculties.

The Loan Application: After the business plans have been drawn up the problem of obtaining funds for the new business must be addressed. Arranging a loan for any company is one of the most complicated transactions in all of business, especially for small companies which are new and growing. Many pitfalls can be encountered when attempting to arrange financing.

Since there is no financial history for a new business, the loan officer must evaluate the soundness of the company's starting point. For example: Is the initial capitalization adequate given the company's business plan and the amount of financing requested? Is there clear-cut management control of the business at the outset or is ownership spread among a group of persons such that control could shift, causing management instability as the business develops? A straightforward presentation of such information, along with a simple balance sheet listing assets, liabilities and equity at the opening of the business will enable the loan officer to answer these questions. Personal financial statements of the firm's principals are also usually requested along with credit histories.

One of the most frequent problems encountered by many entrepreneurs is the fact that obtaining an initial bank loan for a business does not in any way ensure that larger, more important loans for expansion will be available from the same bank one or two years later. Further complicating the financing of a business, the owner often finds that it is considerably more difficult to arrange an expansion loan with a new bank than the one with which his or her company has been dealing.

As a consequence, some small companies find they are able to fill only a portion of their precious sales demand because of their "sudden" credit limitations. Even worse, some companies can get into extreme cash flow difficulties, even bankruptcy, because funds are invested in expansion in anticipation of additional bank financing, which later turns out to be unavailable. These situations develop because initial loans of $10,000, $25,000, or even more made by a bank are based on some specific collateral consideration, such as net worth of the entrepreneur or some asset of the business. These loans are often made by a branch manager whose primary responsibility in the bank is new business development and whose loan approval authority is exhausted by the amount of the initial loan. Often little or no financial analysis of the company is made initially by the bank because the loan is small and fully secured. Later, when expansion creates increased loan requirements, the application is referred to a more senior loan professional, who reviews the company's financial condition far more rigorously. Invariably the sales expansion has pushed the company's loan requirements beyond the collateral considerations which justified the initial loan, and the new request is declined at the very time when the loan is crucial for the future of the business.

Perhaps fifty percent of all small businesses have this problem within three years after they begin operations. It is only one of the many pitfalls in arranging financing, all of which exist primarily because entrepreneurs need substantial amounts of other people's money to run their businesses. Yes, banks and other sources of financing earn interest on the loans which they make, but the failure rate of small businesses is high, and one bad loan can wipe out interest earnings on a large number of small loans. In addition, the administrative costs of small loans are high in proportion to the cost of administering large loans to established companies.

Within this context, a loan application from a small business, except for the small, initial loans with ample collateral just mentioned, will be carefully and cautiously reviewed by a loan officer. Frequently the final decision is made by an officer who has had no personal contact with the applicant. As a consequence, obtaining the loan can be extremely difficult. For this reason it is imperative that the owners and/or management of the company do a thorough and professional job of preparing their presentation for financial assistance. A good presentation rarely can convince a loan officer to make a questionable loan, but a bad presentation can deter that loan officer from making a workable loan. Often a loan to a small business is a border line yes/no decision for the loan officer because of the lack of financial history, unclear profit trends, undercapitalization and on and on. An effective, competent presentation by the applicant can be instrumental in reaching an agreement with the bank.

This is so because a good financial presentation demonstrates to the loan officer that the company management grasps the management requirements of the business at the present time and for the foreseeable future. A good presentation for financing is a clear and complete statement of a good business plan. The business plan delineates the key elements for effective marketing, operations and financial management. It should leave no major questions about the company's operations or finances unanswered, thus giving the banker as complete an understanding as possible. The banker can then be more aggressive in making the loan decision, especially if the entrepreneur has demonstrated a sound grasp of the management requirements.

What Has Been Done To Ease Market Entry? Federal Government assistance to the small business community is most readily available from the Small Business Administration. Assistance can be obtained in several forms: written brochures, both free and priced, SCORE and ACE consultations, and referral assistance. Another government sponsored program designed to assist the small business entrepreneur is the Office of Minority Business Enterprise at the Department of Commerce.

The point of mentioning these agencies at the entry phase of business is that entrepreneurs often want advice that is difficult or embarrassing to ask for. Entrepreneurs may well assume the posture that to ask these questions of their banker or friend would be interpreted as a weakness. Therefore, the need for a non-threatening atmosphere which encourages a free exchange of ideas and experiences is at least partially met through such vehicles as state and local chambers of commerce and local offices of the SBA and OMBE. Available resources can be divided into free and "for a fee," government and free enterprise. One should not necessarily draw a correlation between free and government assistance or "for a fee" and free enterprise assistance. Many accountants, financial planners, lawyers, insurance agents and bankers will agree to an initial interview with a prospective client to discuss her ideas and plans, free of charge.

Insurance

Small and medium-sized businesses are often more vulnerable to the impact of loss than are larger firms, because small operations do not have extensive resources to fall back on to cushion a severe loss, nor can they ordinarily afford to retain a lawyer to defend them against potentially damaging lawsuits. The small business owner needs the financial protection of insurance to assure the continued operation of the business following a serious property or liability loss.

Insurance agents and brokers can be sources of business planning assistance. And, since few businesses are solely financed by savings or family contributions, it makes good sense to include an assessment of the business's exposure to potential financial loss in the business plan presentation.(31) This will not only supply evidence of the entrepreneur's financial management ability to the financial institution, it will also enhance her conception of the day-to-day operations of the business.

Commercial insurance is readily available from thousands of agents and brokers.(32) The commercial insurance market is quite competitive, and different companies offer different rates. Some insurers specialize, prefering to solicit certain types of companies or to emphasize particular coverages. The only rule in selecting insurance is that the prudent business owner should be aware of the existing coverage alternatives. Commercial insurance coverages are most commonly categorized as either surety bonds or property and liability insurance.

Surety bonds will only be briefly addressed here since they are more appropriately related to procurement through contractual arrangements. For the purpose of clarity, surety involves three parties in a contract through a bond issued to a contractor, the "principal," whose satisfactory performance under the contract with the contracting agent, the "obligee," is guaranteed by the "surety," the third party to the contract instrument. Surety is not insurance. If its whole role is to be completely understood, it must be viewed in the light of pre-qualifying a contractor so he or she can secure a contract for which he or she is primarily liable. Surety should not be confused with any form of insurance policy or the contract, itself.

The Study Team queried six surety companies relative to their experience with woman-owned businesses. All companies responded that "no one wants to write the first bond whether to a woman-owned or male-owned business, surety is blind to sex." The familiar analogy was drawn "if you can prove you don't need the loan, the bank will lend you the money." The underwriting process in surety is similar to the financial analysis of the bank loan officer and the "three C's" of character, capacity, and capital are stressed as well as the track record of the business in the respective field. Most small businesses have difficulty meeting the stringent criteria. All six firms stated that it has to be cost-effective for them to underwrite a business and that this is often not the case with a small business. Although, one rather large firm did offer surety to small business firms at a high premium. Requests from small businesses were usually referred elsewhere, such as to the Small Business Administration.

When a business owner cannot obtain the required surety bonding, she is precluded from competition for contracts. This barrier would particularly impact the new, small business owned by a woman.

Property and liability insurance are generally sold in a comprehensive policy although one can be purchased without the other.(33) The price of property/liability insurance is based on two components: the expense factor (including the agent's commission) and the loss factor (based on the projected claims). The loss component is the pure cost of the insurance and is frequently calculated using the combined experience of a large number of companies which pool their statistical data in order to estimate the anticipated losses on a particular class of risks.

Sex is purportedly not a factor in establishing rates in commercial insurance but it is an integral factor in determining eligibility.(34) Does the insurance industry target market the women-owned business? Does the insurance industry deem the women-owned business a viable segment of the business community? The Study Team surveyed property/liability insurance agents and brokers as well as the various trade associations across the country. The response to these questions was generally "No." The female agents/brokers responded that they do seek out the woman-owned business for their portfolios. Eight out of ten of the male respondents explained that "business is business" and that they would not consciously seek to exclude a woman-owned business as a client.

Disability income insurance and medical insurance are ancilliary costs of doing business, whether directly for the woman business owner or her female employees. Disability income insurance and medical care insurance as offered by the insurance industry are replete with discrimination toward women in all three categories of (1) premiums, (2) underwriting practices (the selection of insurable risks), and (3) policy terms and conditions.(35) It has been well documented that these coverages are not equally available to women as to men (see Task Force reports to the respective Insurance Commissioner's of California (1975), Colorado (1975), Iowa (1975), Michigan (1975), New York (1975), and Pennsylvania (1974)). Denial of equal access to insurance at fair rates affects the economic status of all women. It touches employment discrimination, opportunities to hold a job, ability to maintain a family in the face of personal catastrophe, and economic security. Other economic disadvantages of women can be magnified by discriminatory, inadequate, or prohibitively costly insurance.

What is being done to ameliorate the high cost of insurance and to encourage non-discriminatory marketing practices? For approximately eighteen months, the Department of Justice, on behalf of and at the request of the Task Force on Antitrust Immunities of the Economic Policy Board, conducted a study of the insurance business.(36) This study focused primarily on property/casualty lines and addressed the question of whether continuation of the present exemption of the insurance business from federal antitrust laws, by virtue of the McCarran Act and state regulation, is in the public interest.(37) Essentially, it was necessary to determine whether thirty years of state regulation has provided the public with the benefits normally attributed to competition, i.e., reasonable prices based on the cost of rendering the services; efficient services rendered at the lowest possible cost; and innovation -- the utilization of new or improved products or services and methods of distribution. The underlying premise of the study was that, if regulation had not provided these benefits, or if it now appeared that the application of the federal antitrust laws would not interfere with the basic policy objectives of insurance regulation, then legislation should be introduced to modify the statutory antitrust exemption.

The Department of Justice Study Group observed that over the past ten years, a number of states adopted an open competition system of rate regulation after attempting to administer highly regulated systems. The study revealed that the long-run experience of at least one major insurance state (California) under an open competition system, in which the state has relied on market forces to control prices, suggests that unrestricted price competition can provide an effective substitute for rate regulation as a means of achieving reasonable prices and maximum efficiency in the sale and distribution of insurance. A comparison of the experience of the same insurers under certain open competition and prior approval systems suggests that competition fosters independent pricing, operating stability, and flexibility in the pricing structure.

In commercial lines, the findings of the Justice Department indicate that state regulatory schemes are largely illusory and that insurers are generally free to set their own prices, owing to the availability of state-authorized rating plans which permit insurers to price risks individually based essentially on their business judgment and competitive pressures. The prevalence of these plans in commercial lines raises a fundamental question as to the purpose and need for state rate regulation in these lines of insurance.

The study concluded that (1) the insurance industry should be able to conduct its business without any special exemption from the federal antitrust laws, (2) antitrust precedent indicates that insurance companies could pool their loss experience through a statistical bureau consistent with federal antitrust standards, (3) federal antitrust laws would not prohibit any necessary trending of future losses on a composite basis by advisory organizations that were independent of the companies they were serving, and (4) the antitrust laws would not prohibit those voluntary risk-sharing arrangements such as insurance pools and reinsurance agreements, that either were necessary to the conduct of business or served some other legitimate business purpose without substantially lessening competition.

While the Justice Department's report did not propose definitive measures for this dual regulatory system, it did propose measures which are akin to depository financial institutions, involving federal chartering and a related guaranty system. Thus, insurance companies would have the option of seeking a federal charter and thereby losing the McCarran Act protection, or retaining that protection under a state charter and remaining subject to the full scope of state regulation.

The study also noted that competitive restraints may not prevent invidious discrimination in which individuals are denied coverage or are charged disproportionately high rates based on their age, sex, and race. Consequently they recommended federal legislation that would prohibit invidious discrimination in the sale of insurance and that would require validation of risk classes based on age, sex, and race and provide relief against risk classifications that are, among other things, arbitrary or illogical. It follows, then, that federal disclosure requirements with respect to pricing and underwriting experience are not only an important complement to these anti-discrimination measures, but are essential to the full and fair exchange of information in a competitive environment.

Currently, there are two bills pending in Congress which address the repeal of the McCarran-Ferguson Act. They are S. 1710 introduced by Senator Brooke on June 16, 1977, and H.R. 7623 introduced by Representative Downey on June 6, 1977. As of the writing of this report both bills are "in subcommittee." The Study Team believes that passage of either S. 1710 or H.R. 7623 would significantly improve the availability of reasonably priced insurance for the woman-owned business.

3 CAPITAL FORMATION

The Task Force questionnaire (see Appendix) asked questions designed to assess the extent to which predicted variables actually influence the availability of funds for women-owned businesses. For example, questionnaire respondents were asked to indicate all sources of capital used to obtain their businesses and also the total amount of capital obtained. The results of summing responses by loan categories are quite interesting, as can be seen in Table 1. (We realize that summing probably resulted in double-counting capital amounts for those responses where more than one category of capital sources was checked, but feel the data can still be useful in a gross sense.)

According to the data, 67.3 percent of the capital used to start-up the businesses of respondents came from "angel money," *i.e.*, it was obtained from savings, family, and friends. This was true at the larger amounts of capital as well as the smaller. The amount of capital needed to start the business was $15,000 or less in 51.7 percent of the responses. Even at these relatively small amounts, 22.7 percent of the money came from loans (both public and private sector financing). The size of the capital needed by the respondents supports what the study team heard from the bankers they interviewed; women do not usually own businesses, they own *micro-enterprises*. The data indicate that smaller loans are available to women. Bankers we interviewed stated that this is not so because small loans are too expensive to administer. Perhaps the smaller loans were obtained from smaller banks outside large, metropolitan areas.

Venture capital firms appear to play a very small role in financing new women-owned businesses. Such firms usually make larger loans to larger organizations, but our data do not show such a pattern with 13 of the 17 fundings of $50,000 or less.

TABLE 1

How Capital Was Obtained By Amount Obtained Women Business Owners

	$1,000 to 5,000	$6,000 to 15,000	$16,000 to 25,000	$26,000 to 50,000	$51,000 to 75,000	$76,000 to 100,000	$101,000 and Over	Row Total	(Row Percent)
PERSONAL SAVINGS	469	267	148	128	61	213	43	1,191	(34.9%)
JOINT SAVINGS	172	106	64	82	29	23	30	506	(14.8%)
FAMILY	142	98	65	51	20	14	25	415	(12.2%)
FRIENDS	62	47	31	17	11	5	10	183	(5.4%)
GOVERNMENT PROGRAM	17	65	68	113	41	24	39	368	(10.8%)
COMMERCIAL BANK LOAN	146	166	116	148	55	34	70	735	(21.5%)
VENTURE CAPITAL FIRM	2	5	4	2	2	1	1	17	(0.5%)
COLUMN TOTAL	1,010	754	496	541	219	144	250	3,415	
(COLUMN PERCENT)	(29.6%)	(22.1%)	(14.5%)	(15.8%)	(6.4%)	(4.2%)	(7.3%)		(100.0%)

SOURCE: Task Force Questionnaire

The questionnaire data was used to assess the extent to which a woman's marital status influences her ability to obtain capital and credit, as this was a problem area often raised in Congressional hearings, magazine articles, and interviews.

Even considering the uneven numbers of responses in the different marital categories and the very small numbers of responses in some of the cells of the table, marital status appears to have little, if any, relationship to the amount of financial capital obtained to become a business owner (see Table 2). Another way of saying this is that married women do not seem to have an advantage over non-married as far as having access to greater amounts of capital. The proportion of business owners who are unmarried is high at 40.3 percent of the respondants in comparison to what we would expect the population of all women to be. Observations about the pattern of distribution would be more meaningful if a sample of men owners were available for comparison.

This chapter of the report describes capital formation beyond that capital obtained from personal savings, family, or friends, where <u>most new small businesses get their money</u>. We discussed earlier that women are at a disadvantage in building a capital base because they do not ordinarily have as high an income to generate savings as men. It may also be more difficult for women to borrow money from family and friends because of role expectations. These societal influences may very well be the greatest barriers to capital formation for women, particularly in light of the fact that very small businesses are usually not in the target group serviced by venture capital firms. To build the whole picture one must consider not only the sociological issues and the operations of venture capital firms, but also the availability of money for venture capital investment. This topic is discussed in this chapter as well as the chapter on taxation.

Availability of Capital

The woman who seeks capital for her business has potentially available to her the same sources of capital as those available to her male counterparts. In many cases the woman-owned small business collapses, falters, or never gets started because the owner is unable to make full use of these sources.

TABLE 2

Percent Distribution of Responses: Current Marital Status By Amount of Capital Obtained Women Business Owners Only

	$1,000 to $5,000	$6,000 to $15,000	$16,000 to $25,000	$26,000 to $50,000	$51,000 to $75,000	$76,000 to $100,000	$101,000 and Over
Never Married (N = 257)	41.6%	28.0	10.9	10.5	3.5	1.6	3.9
Married (N = 1288)	34.9	21.0	13.0	16.8	5.7	4.0	6.0
Divorced (N = 423)	37.1	25.0	10.0	11.0	4.0	3.1	5.6
Separated (N = 57)	35.1	21.0	5.3	15.9	1.8	5.3	7.1
Widowed (N = 148)	32.4	23.6	10.1	14.9	5.4	4.1	9.6

Total responses = 2173

SOURCE: Task Force Questionnaire

Personal savings and loans from family, friends and the local bank, are most often the sources of start-up funds for a woman's business, as they are for small business in general. Once started, the growing small business is supported by continued bank financing and, if potential for profits is great enough, by venture capital and public equity financing through the selling of common stock in the company. If the enterprise successfully passes through this difficult stage of rapid expansion and heavy dependence on external financing, it emerges as a mature business. The rate of growth slows and stabilizes, and increased profitability combined with more moderate growth finally permit capital needs to be met, at least in part, by internally-generated funds.

The extent of specific knowledge a woman may have about obtaining financial support from these various sources and her persistence in seeking such support are factors which bear heavily on her success in obtaining funds. These are factors she can influence. Beyond the enterpreneur's control, however, are general economic conditions and the state of the capital markets, which generally determine the amount and terms on which investment funds are available, and which help shape the investor's predisposition toward the entrepreneur. These macroeconomic forces and their effects on small business have particular claim on the attention of government bodies interested in assisting women in business, and an understanding of general conditions in the capital markets can aid the businesswoman in planning her capital outlays. For this reason, this section takes the macroeconomic view, and is a preface to the greater detail which follows.

<u>The "Capital Shortage" for Small Business</u>: In view of the recent recession and a presently hesitant economy, it seems paradoxical to speak of "capital shortage." However, a shortage of funds for small business indeed appears to exist, and it results from a concentration of size and influence within the business world and the capital markets, and from the high degree of uncertainty surrounding current economic decision-making.

Conditions in the stock market have been bad for several years, especially for new issues of stock by small companies, and small companies typically cannot fall back on the pools of internally-generated funds or the relatively easy access to bank loans and other external sources that larger corporations are able to use in place of public equity financing. Evidence of the problem is sobering. February 1978 hearings by the Senate Select Committee on Small Business revealed that companies making their first stock offering accounted for a healthy 633 in 1972, or 62 percent of new issues in that year, but this group dwindled to 42 in 1976, or only 16 percent of new issues.(38) John P. Birkelund, President of New Court Securities Corporation, a New York-based investment banking concern, wrote in the February, 1977 Dun's Review, "...medium sized and smaller corporations are attracting a substantially lower proportion of the trading on securities exchanges than four years ago, when we were at a similar stage of economic recovery."(39) He remarked further that, at the time he was writing, many stocks were still selling above the issue price.

Small businesses hoping to enter the market, yet faced with these conditions, are forced to reassess their plans. For small business, the effect of limited access to the new issues market and of weak stock prices is to reduce the potential for expansion as independent concerns. If entrepreneurs cannot succeed with a public offering, they must try to sell stock to friends and acquaintances, reduce growth and capital needs, or sell out to a larger firm.

Reasons for the "capital shortage" faced by small businesses are several. The most pervasive cause is the trend toward bigness in the U.S. economy. Investment decision-making is being carried on by fewer individuals. More than ever, savings are being directed to large institutions (money-center banks, pension funds, mutual funds) whose officers place funds in large, well-established businesses, rarely considering the smaller firm as an investment possibility.

This trend toward concentration of investment decision-making has been largely responsible for the reduced opportunities awaiting the small company in the stock market. When the stock market plunged in 1974, the small investor dropped out of the market and, still remembering his losses, has yet to return in force. Meanwhile, institutions have been trading in record volume. A significant difference between these two classes of investors is that small investors are often willing to trade in the shares of small companies, while institutions as a rule are not. The disinclination of institutions to trade in small companies stems from two causes. First is the obvious one of size. The average trade for an insurance-company or pension-fund account may well run hundreds of thousands of dollars. For most companies listed over-the-counter or on the American Stock Exchange, a buy or sell order of this magnitude would be equivalent, or nearly so, to the entire volume of a company's outstanding shares, and if executed could cause extreme disruption in the market for such a company's stock. The Securities and Exchange Commission and the stock exchange discourage market disorder, with the result that institutions shy away from small-company stocks.(40) The second cause of this behavior by institutions is the Pension Reform Act (ERISA) of 1974, which seeks to limit the risk in pension-fund investment. The law appears to be effective: a survey of pension-fund and employee-benefit officials found that 60 percent were less willing, after ERISA, to invest in anything but blue-chip and fixed-income securities.(41)

Competition in the brokerage industry, leading to numerous failures and mergers among brokerage firms, has further concentrated economic activity in the stock market, to the detriment of the small business seeking equity finance. Many of the broker-dealers which have failed in recent years were regional firms, the traditional underwriters of new stock issues for small, local companies. The larger brokerage houses remaining, especially those based in New York, are reluctant to spend time and money in bringing out a small stock offering. According to one estimate, major Wall Street firms now handle stock offerings only for companies with more than $1 million in profits, a figure small businesses cannot match.(42)

In recent years, the availability of venture capital to the entrepreneur has also been reduced, the result of various developments. Venture capitalists had typically expected to realize their greatest returns by investing in a small business to give it the financial strength for rapid growth, then, within a couple or three years, introducing an issue of the company's stock to the market and reaping a handsome return on the initial investment. However, due to the problem of reduced opportunities for small companies in the stock market and the market's general price weakness, this formula is now rarely successful.

In another development, it now takes a larger initial investment to see a venture through its infancy and the time to fruition is longer. For example, Dun's Review reports the estimate of Paul Wythes, a partner in the Palo Alto firm of Sutter Hill Ventures, that the typical investment his firm makes in a new company has increased to $700,000 in 1977 from $300,000 five years before. Another venture capitalist, Arthur Rock of San Francisco, credits part of the escalation in cost to inflation, but also cites, according to Dun's, "a sharp increase in the complexity of equipment needed in a modern plant and a stretch-out in the time required to produce a new product because of the close tolerances."(43)

The inducement to venture capitalists has always been a high-risk, high-reward combination, but now these various economic and technical conditions have warped the risk/reward ratio. Risks are high, yet the size and immediacy of possible returns are reduced. Consider that during the 1960's a venture capitalist could hope to recover ten to thirty times his investment within two to three years. Now the figures have changed to ten times an investment recovered in five to seven years.(44) Not surprisingly, venture capitalists have reacted to these changed circumstances by making less venture capital available for start-ups, the riskiest phase of a venture. Venture capitalists are increasingly interested in supporting small companies already in their portfolios, and in investing in under-valued stocks of small companies already trading in the market. Those venture capitalists who would formerly have sold stock to the public when a venture was ready to pay off now sell the entire company to a single purchaser, usually a large corporation. Indeed, a few giant corporations are now conducting their own venture capital operations.

The potential for both stock-market and venture-capital investors to take an interest in small companies has been adversely affected by Federal tax and regulatory policy. Most evidently damaging has been the movement of capital gains tax rates toward the level of tax rates on regular earned income. This subject will be discussed later in this report. As this happens, the tax incentive to invest is severely weakened. All businesses seeking funds are affected, but small businesses, with their limited resources and alternatives, are, perhaps, most vulnerable.

Bank financing is another problem. In many cases the small-business owner searches no further for funds than the local bank, not feeling the need to tap the larger pools of capital in the stock or venture-capital markets. Even so, she may well be caught by limited availability of bank funds, since a small business in need of capital may quickly reach the limits of prudent debt financing, which bankers will be unwilling to surpass. This problem is often shared by small businesses which seek public equity finance and are rebuffed by the stock market; having been frustrated in their attempts to broaden the equity portion of their balance sheets, these companies find that, for this very reason, they are unable to persuade bankers to lend substantial amounts of new money. Simply put, the growth prospects of these companies are stunted.

At the same time and strangely enough, a few well-established but small companies are finding bank funds plentiful. Beginning in 1975, large corporations worked to redress their borrowing excesses of 1973 and 1974 (when the prime rate averaged an astounding 10.81 percent, according to Commerce Department data). As these corporations strove to develop alternative sources of finance more fully, their demand for bank loans dropped. Nonfinancial corporations actually paid down bank loans in 1975 and 1976, and large money-center banks are still troubled by low demand from these customers. The result is that a number of the large banks have begun seeking business customers from the so-called "middle market" of firms whose sales fall in the $2 million to $100 million range. At the very low end of this range are the small businesses. For companies of this size, connection with a large money-center bank had been highly unusual. Financial advice and other services may accompany these small companies' loan accounts with the big banks, and, for the moment, their financial needs appear to be satisfied. There can be a degree of danger in this situation, however, for if loan demand from large corporations picks up again, the money-center banks may no longer need the business of their smaller clients and new loans or refinancings may no longer be forthcoming from this source. This was the situation in the early 1970's, and the small company with limited financial alternatives is ill-equipped to deal with this situation.

Capital Availability for the Woman Business-owner: The "capital shortage" is a condition encountered by small business in general, but how greatly does it affect the woman business-owner? Information is scarce, but some tentative conclusions seem reasonable. The Commerce Department reports, as a result of its 1972 survey, that two-thirds of women-owned businesses were concentrated in the following ten industry groups, arranged in descending order of gross dollar receipts for each group: eating and drinking places (average gross receipts per firm, $36,000), miscellaneous retail operations ($15,000), food stores ($52,000), automotive dealerships and gas stations ($92,000), personal services ($9,000), real estate ($13,000), apparel and accessory stores ($43,000), special trade contractors in the construction industry ($26,000), business services ($10,000), and hotels and other lodging places ($16,000).(45) Generally speaking, small businesses in this group of industries turn relatively low profits and have modest growth potential, and thus are not the enterprises most likely to need or attract capital. As can be seen from the receipts figures, most of the women-owned businesses are very small. For most of these women, it is simply not realistic to contemplate venture capital participation or public stock offerings, and conditions in those markets are irrelevant to their operations. However, there are exceptions to this generalization, and over time there surely will be more. Those female entrepreneurs in highly profitable industries, cosmetics, for example, or businesses in the health field, with the potential to grow to corporate maturity, face the same capital-shortage problems as male entrepreneurs.

There are signs that women's businesses as a group are far from fully engaged in the financial arena. Although the development of women's businesses has hardly begun, the future offers possibilities. In the years ahead, the greatest opportunities for profitable, financeable businesses in the U.S. may well shift toward the development of labor-saving innovations and communications advances, as growth of the labor force slows; and toward leisure activities and more personalized and luxurious consumer goods and services, as the number of workers per household and income per household increase.(46) Although women compete in all fields of enterprise, these latter areas are ones in which women may expect to do especially well, judging by the present distribution of their businesses, with retail and service operations predominating. Sound enterprises in these growth areas, managed with purpose and vision, will be likely to attract financing. The major question is whether or not the forms in which financing is available to the small businesswoman will permit her to retain ownership control of the company throughout its growth years and into maturity. If capital markets developments in recent years are any indication, the road to financial growth for small enterprises may lead increasingly to merger or acquisition agreements with larger firms.

The probable effect of these trends on the economy is a matter of conjecture. Certainly the economy can only benefit as more women come to develop their talents, including entrepreneurial talent, more fully. However, the problems of financing the small business in the shadow of relatively concentrated economic power may dim the enthusiasm of potential entrepreneurs for embarking on the arduous course of small-business ownership.

Regulation A and Other Stock Issues

As noted earlier, small companies are practically foreclosed from the public securities markets, in large degree because of government controls. As a result, even those with more fortunate and aggressive management may find themselves in desparate need of equity capital and with unfavorable means of acquiring the capital except by merging into a larger company.(47) We would only amend this statement to state affirmatively that small companies are currently closed out of the securities market.

Effect of Federal Securities Regulation on Capital Formation by Small Business: Public debate has centered on three separate ways in which Federal securities regulation impacts small businesses: (1) regulation of public offerings, (2) restriction on resale of securities exempt from the registration requirements, and (3) periodic reporting under the Securities Exchange Act of 1934.

1. Regulation of Public Offerings

The first area is the regulation of the public offerings of securities under the Securities Act of 1933. The registration costs of new issues appear to be proportionately larger for small businesses, which generally raise capital through small offerings. It is estimated that the cost of preparing the required registration statement is approximately $240,000.

Recent efforts by the Securities and Exchange Commission to ease the burden of the registration requirements have tended to help larger, more established companies, which already have outstanding registered securities that are traded publicly and, therefore, are subject to the comprehensive periodic reporting requirements of the Securities Exchange Act of 1934. This is because the SEC has attempted to integrate the 1934 Act reporting requirements and the registration requirements for new issues. These efforts have not lessened the burden for smaller, emerging companies because they do not report under the Securities Exchange Act of 1934.

In response to the concerns over the impact of existing registration requirements on small companies, the SEC has proposed a new registration form (Form S-18) under the Securities Act of 1933 which would reduce the narrative and financial statement disclosure requirements of sales of securities not exceeding three million dollars.

Exempt Offerings: Because the cost of a full blown registration is proportionately larger for small issues, most small businesses seeking to raise capital from the sale of securities look for alternatives to registration with SEC. One major alternative relied upon extensively by small businesses, as well as large companies, is the issuance of securities in a private offering that is exempt from the registration requirements of the Securities Act of 1933.

Private Offering Exemption -- The rationale of the private offering exemption is that registration should not be required where there is no practical need for it or where the public benefits of registration are too remote. Accordingly, in determining whether an offering is a non-public offering exempt from registration, the courts have focused on whether the offerees and purchasers of the offering have access to the kind of information that a registration would disclose, possess the necessary sophistication in financial matters to evaluate the offer intelligently, and generally are able to fend for themselves. However, until 1974, the SEC never set forth with any specificity the requirements for the private offering exemptions, and, thus, issuers faced uncertain risks in attempting to rely on the exemption.

In 1974, the SEC issued Rule 146 in an attempt to remove these uncertainties by setting forth specific "safe harbor" criteria, which companies could satisfy and be reasonably certain of qualifying for the private offering exemption. Rule 146 specifies that the offering must be limited to 35 purchasers and requires that the issuer have reasonable ground to believe, prior to making any offer of sale, either: (1) that the offeree has sufficient knowledge and experience in financial and business matters to evaluate the prospective investment; or (2) that the offeree is a person who can bear the economic risk of the investment.

In addition, the rule requires either that each offeree have access to the same kind of information that is required in a registration statement under the Securities Act of 1933, or, if an offeree does not have access to such information, that the issuer furnish it to him. The Rule permits companies that report under the Securities Exchange Act of 1934 to satisfy its disclosure requirements by simply furnishing the purchaser or offeree with the information contained in their most recent filings under the 1934 Act, such as their latest annual and quarterly reports, and their most recent proxy statements.

While Rule 146 has worked reasonably well for larger companies, which are registered under the 1934 Act and have established investment banking relationships, some commentators have maintained that it has restricted the ability of small companies to use the private offering exemption. They point out, for example, that the disclosure requirements of Rule 146 appear to bear more heavily on the small issuer.

While companies subject to the periodic reporting requirements of the 1934 Act may find it reasonably convenient to supply the required information, many small companies that are not subject to the 1934 Act may find the cost of supplying the information required by Rule 146 to be nearly as great as the cost of filing a registration statement.

Some observers also contend that the Rule's requirements with respect to the qualification of the offerees and purchasers disadvantage the small issuer. For example, it is argued that issuers still face uncertainties under the Rule in determining whether a prospective purchaser of a private offering possesses the requisite knowledge or financial expertise to enable him to evaluate the returns and risk of the investment. The uncertainty in this regard is more likely to hurt the small issuer than the larger issuer because small companies rely more heavily on individual investors than on institutional investors, which can readily meet the qualifications of Rule 146.

As noted above, Rule 146 does permit a small issuer to offer securities to unsophisticated investors, provided they are able to bear the economic risk and are represented by an "offeree representative" or group of representatives, who possess the requisite financial and business expertise. Commentators claim, however, that the use of offeree representatives may prove cumbersome and costly in small offerings. They contend that most likely offeree representatives will be registered investment advisors or investment banking firms experienced in evaluating issuers. They claim that attorneys and accountants may not have sufficient investment expertise to qualify as offeree representatives under the Rule. In addition, attorneys not previously registered may be reluctant to subject themselves to the Investment Advisors Act, as the SEC apparently has required where an attorney serves as offeree representative.

Small issuers may not be able to obtain the services of an investment banking firm to act as an offeree representative for a variety of reasons. For example, the size of the offerings may not justify the cost of the required detailed investigation of the issuer by someone with sufficient expertise to serve as offeree representative.

Small Issue Exemptions -- The Securities and Exchange Commission has established two exemptions for small issues under section 3(b) of the Securities Act of 1933, which authorizes such exemptions for offerings of $500,000 in stock or less. The first is Regulation A, which provides an exemption from the registration requirements for small issues involving not more than $500,000. Under this regulation the issuer must file an offering circular ten days in advance of the sale at the appropriate regional SEC office, the issuer is free to sell the securities without any limitations on their sale or distribution. Moreover, investors receiving securities in a Regulation A offering can resell them without restriction.

Critics, however, contend that this exemption has its disadvantages. First, they complain that the total amount of capital that can be raised is limited to $500,000, which does not permit equity financing at an efficient level. Secondly, they contend that the Regulation A offering circular has become increasingly complex to prepare so that its overall costs on a percentage basis are not substantially less than a full registration. The SEC is currently reviewing the $500,000 limitation of Regulation A to determine whether raising of the limits may be justified in light of the rate of inflation in recent years.

The second small issue exemption is Rule 240, which the SEC promulgated in 1976. Rule 240 permits an issuer, in any 12 month period, to issue to the public without registration up to $100,000 of its securities, as long as immediately after and before each sale the securities are not beneficially owned by more than 100 persons, and so long as no advertising is employed and no remuneration is paid in soliciting sales. The Rule places no limit on the number of purchasers or on their qualifications to evaluate the investment or to bear the economic risk. Moreover, unlike Rule 146, Rule 240 does not require any formal disclosure, but relies upon the antifraud provisions of the securities laws to protect investors. The Rule merely requires the issuer to file notification of an offering on Form 240 with the regional office within 10 days of the close of the month in which the sale is made.

The $100,000 limitation does not apply to securities sold to executive officers, directors, promoters and employees of the issuer, or to non-convertible debt securities sold to certain enumerated institutional investors. Therefore, it is possible to raise in excess of $100,000 under the Rule so long as only that amount is raised from the public.

While Rule 240, on the whole, solves many problems for small businesses in issuing securities, it is argued that the Rule has limited utility because of the $100,000 limitation. On the other hand, Rule 240 has been criticized on the ground that it does not adequately protect investors because it does not require the provision of information.

2. <u>Restrictions on Resale of Securities Exempt from the Registration Requirements</u>

Thus far, we have focused on the problems of the small issuer in seeking an exemption from costly and lengthy registration procedures. However, other securities regulations restrict the resale of securities issued by a small business under the private offering or Rule 240 exemptions. To the extent that these regulations restrict the ability of investors to sell their investments in small businesses, they tend to reduce the liquidity of such investments, and thereby impede the flow of capital into small business and venture capital investments.

Rule 144 is the principal SEC regulation governing the resale of securities purchased by investors in transactions exempt from registration. The rule is designed to insure that purchasers of securities in transactions exempt from registration (restricted securities) do not act as conduits for the sale to the public of unregistered securities of issuers concerning which adequate current information is not available to the public.

Thus, Rule 144 prohibits the resale of securities received in transactions exempt from registration, unless certain conditions are met. First, the purchasers must hold the securities for a minimum period of two years. Second, the issuer must be subject to the periodic reporting requirements of the Securities Exchange Act of 1934 for at least 90 days prior to the sale of the securities, thus assuring the public availability of information concerning the issuer.

Finally, the securities must be offered in such a manner and in such quantities as to not disrupt the trading markets. Thus, the securities can only be sold in normal trading transactions with no unusual brokerage commission and the amounts which can be offered are limited. For exchange-listed securities, the number of securities sold by an individual during any six-month period must be the lesser of one percent of the shares outstanding, or the average weekly trading volume. For over-the-counter stock the amount is limited to one percent of the shares outstanding, without a trading volume limitation.

For the small issuer, Rule 144 provides little help because it requires either registration under the 1934 Act or making publicly available information equivalent to that provided in 1934 Act reports. Thus, investors holding restricted securities of small issuers, which do not wish to assume the burdens of registration, generally have to seek other methods of resale, such as a resale in an exempted private offering.

Some have maintained that Rule 144 is overly restrictive even as to those small issuers who are willing and able to bear the costs of registration under the 1934 Act. The SBA Task Force on Venture and Equity Capital(48) concluded that the volume limitations of the Rule are too severe, and seriously impair the ability of venture capitalists and other professional investors to free up capital for other investments. The Task Force's recommendations have given rise to proposed legislation, pending before Congress, which would relax certain provisions of the securities laws and regulations that affect small issuers. This legislation includes proposals to raise the statutory ceiling of the small issue exemption in section 3(b) from $500,000 to $3 million, and liberalize Rules 144 and 146. The SEC is currently reviewing the volume and sale rate limitations set forth in Rule 144.

3. Periodic Reporting Requirements Under the Securities Exchange Act of 1934

Companies with a class of securities listed on a national securities exchange or those with total assets exceeding $1 million and a class of equity securities held of record by 500 or more persons must register those securities with the SEC. Upon registration these companies become subject to the periodic reporting and proxy solicitation provisions of the Securities Exchange Act of 1934. As a general rule, companies required to file periodic reports with the SEC presently are required to provide essentially the same type and quality of information regardless of their size. Similarly, the present proxy solicitation provisions do not recognize differences among users by size.

Recent Initiatives to Examine the Impact of Federal Securities and Regulation on Small Business: The Study Team asked the Securities and Exchange Commission whether there has been any recognition of the plight of the small business owner in the capital markets. The response was affirmative. That is, the SEC has, within the last year, studied the problem and is planning to conduct public hearings to examine the effect of Federal securities regulations and disclosure requirements on the ability of small businesses to raise capital. As mentioned above, the SEC will examine the effect of the registration requirements of the Securities Act of 1933 on small companies and the effectiveness of various procedures under which small issuers may make securities offerings without filing a costly registration statement. These include the private offering. The second major area which SEC intends to examine is the impact of the periodic reporting requirements of the Securities Exchange Act of 1934 on small companies, and the desirability and feasibility of reducing these disclosure requirements for smaller companies.

While the periodic reporting requirements of the Securities Exchange Act are not a direct cost of a new securities financing, they do impose significant costs which may deter small non-public companies from raising funds in the public markets. The SEC's Advisory Committee on Corporate Disclosure found that the costs of preparing periodic reports were significantly higher for small companies than for medium and large ones. Thus, the Committee recommended that the SEC study whether, and to what extent, it should attempt to reduce the burden imposed on smaller companies by the existing periodic reporting requirements of the Exchange Act. The SEC intended to explore this question in April hearings.

The SEC's Advisory Committee is working closely with the Financial Accounting Standards Board (FASB), the private rule-making body of the accounting profession. The FASB, responding to its constituents, recently agreed to amend FASB Statement No. 14, dealing with reporting requirements, to recognize that differences do exist between large and small businesses, and to reflect these differences in the accounting rules. Thus, there now is an awareness that small and closely held companies are in an economic environment completely different from that of large and publicly held companies.(49)

The Study Group also met with the Treasury Department's Small Business Advisory Committee and discussed capital formation problems of small companies. The committee urged the Securities and Exchange Commission to adopt the following:

1. Increase the ceiling for Regulation A offerings from $500,000 to $3 million;

2. Amend section 12(g) of the Securities and Exchange Commission Act of 1934 to change the criteria for companies subject to the Act's periodic reporting requirements to companies having assets exceeding $5 million and 2,500 shareholders;

3. Relax the volume and rates of sale limitations in Rule 144 governing the resale of securities

received in offerings exempt from registration; and

4. Program SEC's management information system to include the sex of the owner company seeking to go public and those who actually do go public.

Venture Capital Firms

Do women have access to, and are they utilizing the major sources of venture capital which are available to promote business growth? For that majority of women business owners whose businesses are small, there are two possible alternative developments. On the one hand, the firm may fall within the traditional small business category (characterized by low demand for capital, lack of sophisticated technology, and a local geographical market) and, by choice, remain small. On the other hand, the firm may simply be in its beginning stage and have a real potential for growth. It is this type of small business which requires capital and, because of the special riskiness of small business, financing through the use of venture capital markets has developed.

In exploring the area of venture capital, the Study Team came to the conclusion that while venture capital is presently in short supply for <u>all</u> small businesses, women-owned businesses have received less funding of this kind than other small businesses. Respondents to the Task Force questionnaire reported that less than one percent of their start-up capital came from venture capital firms. Further, those institutions which the Federal government has licensed specifically to provide venture capital, such as Small Business Investment Companies, have not succeeded in significantly furthering women-owned businesses.

Venture capital comes from a number of different sources ranging from individual wealthy investors to partnerships, mutual funds, investment development corporations, and others. Recognizing the lack of hard information on women in venture capital markets and in an effort to establish the beginning of a data base on the use by women-owned businesses of venture capital, the Study Team undertook a survey of twenty-six venture capital firms of all types in the major geographical regions of the U.S.

The risks of the small firm are magnified compared to those of businesses in general. Economic conditions, labor costs and competition in the market place all have a more immediate impact. In addition the small firm is more vulnerable because of its limited geographical market and the lack of up-to-date financial advice or management techniques often found in small businesses. Such firms may also be unable to afford modern cost-saving technology. One state-funded study estimated that at least 20 percent of all small businesses fail annually.(50) All firms thus have risks, small businesses have more severe risks, and women-owned small businesses are perceived by the venture capital markets as being even more risky. Reasons given for this include the perception by many analysts that women lack business training, lack a "track record" of business success, and usually select fields of business which are unsuited to the high yield returns which make a risky investment worthwhile.

Where can women business owners turn for venture capital? The tax advantages of capital gains income had made such investments attractive for wealthy individuals until recent changes in tax laws. Private sources of capital range from "angel money" from family and friends to the more structured venture partnerships and companies. Most of these investment companies prefer to buy equity in the company but occasionally participate in financing part of the debt of company. Close ties are maintained between the investors and the client company with the investors frequently represented on the board of directors of the company.

Ninety-seven percent of all businesses are classified as small.(51) Small businesses exemplify the American ideal of the individual in business for himself or herself, fostering independence of thought and thwarting monopoly. In fact, about half the nation's workforce gain their livelihoods from small businesses. Many small businesses provide ideal proving grounds for the development and introduction of new products and technology, and young, high-technology companies had an average contribution of 40.7 percent per year job growth rate from 1969 to 1974 in comparison to a 0.6 percent per year rate in mature companies.(52)

To foster these businesses the Small Business Administration (SBA) was established by Congress in 1953 and several programs initiated including the Business Loan Programs and the Economic Opportunity Loan Program and the Local Development Company Loan Program for economically disadvantaged and low-income areas. More important for women was legislation permitting the creation of Small Business Investment Companies (SBICs) in 1958 and 301(d) SBICs [formerly known as Minority Enterprise Small Business Investment Companies (MESBICs)] in 1972. SBICs are owned privately, either by banks or by operating companies, or are publicly held. Although a $150,000 minimum investment is required to start one, currently SBA's policy is to require $500,000 as initial capitalization; additional funds may be raised by selling subordinate debentures to the SBA. The 301(d) SBICs (MESBICs) were licensed to assist businesses owned by socially or economically disadvantaged persons. SBICs, like other venture capital firms, generally take an equity (or ownership) position in the companies in which they invest, and also provide financial and management advice for a fee. The 301(d) SBICs differ from SBICs primarily in that socially or economically disadvantaged individuals must own and manage at least 50 percent of the client business.

Currently, there are approximately 280 operating SBICs and 87 operating 301(d) SBICs with resources of over $1 billion.

The Study Team's survey of these venture capital financing sources has led us to conclude that major barriers exist that have kept women from participating in this money market. As mentioned earlier, for all types of venture capital firms our most disturbing finding is that venture capital is now shrinking both in the number of underwritings (down from 418 in 1972 to 4 in 1975) and in amounts of capital raised (down from $918 million in 1972 to $100 million in 1975).(53) This decrease is due to a number of factors including:

-- A falling stock market which discouraged investors of all kinds;

-- increased concentration of savings in large banks with conservative investment policies (10 banks now have 33 percent of all deposits);(54)

-- the rapid growth of mutual and pension funds which are constrained from more speculative investment by the Employee Retirement Income Security Act (ERISA);

-- increasing government regulations which discourage small business starts by demanding many statements, surveys, and reports which place a time consuming and costly burden on the small firm;

-- the institutionalization of market trading and the decline in the number of stockbrokers which makes market access more difficult for individual investors;

- -- the prohibitively rising costs of making a public offering; and

- -- the reluctance of investors to place their money in ventures where profits can be maximized only as capital gains or losses, i.e., when a company is sold or goes under. As one investor put it, "There is no compensation for higher risk in the present tax structure." Those interviewed felt that current high capital gains taxes are discouraging investors from withdrawing funds from a successful venture, thus further shrinking the amount of available funds for new enterprises.

The result of these developments has been the drastic reduction in the availability of venture capital, especially for start-up ventures. The consequences for women are particularly serious. If we recognize that few individuals of either sex have the desire, training or experience to expand their own business, and then realize that the critical mass of women-owned businesses from which such managerial types will rise has just begun to gather, we must appreciate the urgent need for funds to be available to encourage start-up prospects.

There are still other barriers to full utilization of that venture capital which is still available. These include:

- -- Women are not fully informed about opportunities for obtaining venture capital. These financing institutions do not advertise. Instead, they rely on word-of-mouth communication in a business network which has traditionally excluded women.

- -- Women business owners are frequently in fields which do not lend themselves to large scale investment which in turn leads to rapid growth, high sales, and an eventual public offering to stock. Economies of scale make loans of at least $150,000 the minimum acceptable to most private venture capital firms. As one analyst put it, "Where is the woman who will walk through my door asking for money to set up a computer software company? I'd fund her in a minute. All I get are boutique owners."

-- Investors do not perceive women as a separate market segment with ideas that might be pursued. One northeast analyst commented, "If I go after women as a target market I'm afraid all I'd do is flush out the beauty parlors."

-- Only five of the venture capitalists surveyed had been approached by a woman business owner seeking funds. Of thirteen proposals by women which were funded in the past two years by these venture capital firms, six have already failed (these were: a building maintenance company, a voting machine manufacturer, a wholesale grocer, two jewelry store owners, and a publisher) while seven are still going (these are: a honey importer, a toy distributor, a typing service, a liquor distributor, a hairdresser, a photography gallery and a construction firm). None of the successful ventures presently shows the potential for taking off in sales and going public through the sale of common stock. Half of the fundings were done by 301(d) SBICs, whose standards of funding selection include criteria other than potential for rapid financial growth.

-- Women lack the background in finance and the business experience which form the basic criteria for accepting and funding proposals. These include what most analysts refer to as a "good track record" or "good tickets," i.e., years of sound business experience and good personal references. As another investment company official expressed it, "Most venture opportunities develop from managers in their late 30's with ten to fifteen years of solid management experience behind them. There are mighty few women in that bracket who want to go on their own. Perhaps only one man in a thousand is willing to leave a large organization, and you can figure out what those statistics mean for the small number of women in business now. However, there are many bright women now starting out and ten to fifteen years will show a big difference."

The picture for women presented by SBIC and 301(d) SBIC funding is even more grim. Our survey disclosed a situation in which many SBICs and 301(d) SBICs are under-capitalized and illiquid. Very few of those surveyed are currently funding proposals and none is soliciting projects specifically from women. There is even substantial confusion among the 301(d) managers over whether women per se are eligible for funding and different responses were given to these questions ranging from, "Sure we'd fund a woman if we ever saw one," to, "We wouldn't fund a proposal from a woman unless she were a member of a racial minority and we haven't seen any of those. In fact, we're out of funds and we're just hanging on, hoping the SBA will save us somehow."

Fairly typical of the venture capital picture is a seven year old southeastern 301(d) SBIC funded at $300,000. It has given only two loans this fiscal year totaling $88,000, neither to a woman. It has taken equity positions in those businesses it has funded, thus giving it no current interest income with which to pay off its $200,000 loan from the SBA ($10,500 interest per year). As a result of its subordinate debt position it has failed to collect when investments have gone sour, and it still must find funds for current operations. The manager admitted, "It's a vicious circle. I don't have the funds to hire good analysts to properly evaluate business proposals and, as a result, I've invested in a lot of businesses that have gone sour." This 301(d) SBIC has had losses of $50,000 to $80,000 every year since 1973 and is only holding out in the hope that Community Development Corporation funds will be available to it in October. The manager added, "I've never seen a woman with a fundable idea."

In sum, SBICs and 301(d) SBICs (MESBICs), as currently structured, were not designed to meet and do not meet the needs of women business owners both in funds available and in reaching out to support and educate women. The trend is not encouraging. For example, while 85 301(d) SBICs are listed as operating, our telephone survey of six found one out of business, one dormant, and a third not answering the phone and presumably dormant. Those still functioning admitted they were not thriving and were not a good current source of funds. One manager commented, "The concept behind MESBICs was more social than economic and we're having to live through the experience of being a social solution. This has given MESBICs a bad name from a strictly economic viewpoint." Another added, "MESBICs were never capitalized properly. They are insufficiently leveraged. They haven't treated minority-owned businesses as businesses but as solutions to social problems."

Recommendations about furthering the entrance of women into money markets are made elsewhere in this report. However, it should be noted that there is strong agreement among most investors in venture capital areas that legislation and tax policy changes can go far in encouraging a reawakening of interest in the field of venture capital. For example, there is general agreement among certain investors that a tax law that would permit a business woman or man to withdraw funds from an on-going business and reinvest them in another within a given time limit without being taxed on capital gains (just as an individual selling a house is not taxed if he buys another within a year) would encourage a new influx of seed money for new projects. Other regulations on depreciation, surtax exemptions, institutional investment regulations, and small offerings exemptions are also needed. These topics are covered in more detail in Chapter 5.

The Deputy Administrator of the Small Business Administration recently testified before Congress:

> In today's markets few small or medium size firms are able to make private placements or go public. With these routes to liquidity closed, and little prospect for near-term realization of capital gains, SBICs must structure their financings to produce income to cover their own expenses.
>
> This means that SBIC financings are increasingly taking the form of loans, or quasi-equity with some fixed repayment features. Thus, the basic intent of the program -- to provide long-term growth capital for small firms -- is not being adequately addressed. Also the small business person is being squeezed into the difficult posture of debt repayment, or equity repurchase, at a time when retention of permanent capital is vital.(55)

Although the statute does not presently allow short-term debt or consumer loans, a few SBICs and 301(d) SBIC managers suggested that SBA ask Congress to restructure the statute to allow them to make more investments in higher return loans such as short-term debt or consumer loans in order to ease their cash flow problems and to meet their interest payments. This would, however, have the effect of simply transferring the interest burden onto the small client businesses who can least afford it.

The Study Team recognizes that while legislation is needed to increase the availability of venture capital, the goal of increasing the numbers of successful women business owners can be approached from another side -- that of funding, training, and encouraging women to become the entrepreneurs of tomorrow. We call for the creation of programs which would carry out the following activities:

-- Identify potential women entrepreneurs,

-- conduct workshops to train and evaluate them,

-- guide and assist them in developing comprehensive business plans, and

-- aid them in securing adequate equity and debt financing.

Some workshops are presently being run on a small scale by a private group in Boston (Institute for New Enterprise Development), some under the auspices of the Commerce Department Office of Minority Business Enterprise. <u>No women have as yet been included in the OMBE program</u>.

To facilitate moving women into the mainstream of business ownership, a mechanism for assisting the transition is needed similar to services provided by OMBE. We suggest using grants or contracts to fund the establishment of local groups. Such a group has been established in Minnesota for minority business. A description of the Twin Cities Model of an Economic Development Organization follows:

Local companies make grants (pledges of funds for five years) to a non-profit entity with a small salaried management group. The funds are used to form a pool of capital and to pay operating expenses. The capital is loaned to small businesses as equity capital. The organization is associated with teams within local banks who become specialized in making loans to the target group. In addition to satisfying the "charitable instinct," there are incentives to such organizations built into tax laws (cf Sec. 501C3 IRS Code). Losses are tax deductible as are the original corporate contributions, which are treated as charitable deductions.

4 CREDIT AND THE WOMAN-OWNED BUSINESS

A respondent to the Task Force questionnaire wrote, "I find that for me, running my own business is much like raising a child. As the child reaches a new stage of development, the parents have new problems to face and handle. Once these problems are resolved everything runs smoothly again until the next stage and the next problem. For right now, things are running smoothly."

The major commercial sources of funds for the established business are described in this section. These are in addition to money from family and friends or from the business owner's "sweat equity."

Equal Access to Credit

The availability of credit to women is vital because it improves their economic status and determines their access to entrepreneurship, and yet inability to obtain credit because they are women has been reported as a problem faced by women business owners. Historically, women have not been able to obtain credit on the same basis as men due to a pattern of lending practices which discriminated against women.(56)

The refusal of credit to women has often been based on societal attitudes, for example, presumptions about women's permanency in the labor force and the unreliability of their income; belief that women do not really need to work because they do not have to support a family, and if they work it is only for "pin money"; assumptions regarding women's job patterns based on the probability of marriage, pregnancy, and childrearing; old-wives' tales that women do not know how to control money; belief in the instability and inability of single and divorced women to control personal affairs; and the attitude that all women need male protection. The social justification for discrimination in the granting of credit to women was that a woman's legal status is inferior to a man's.(57) Though research has shown that women are, in fact, good credit risks, women often have had discontinuous work force experience and low-paying jobs which do not provide the background lenders look for when judging credit applications. Credit discrimination has pervaded all forms of credit: consumer, mortgage, and business credit.(58)

Unfortunately, most of the written materials available on the subject, such as accounts of Congressional hearings and articles, relate to consumer credit; thus, the full extent of the difficulties in specifically obtaining business credit is not known.(59) However, there is little reason to doubt that many of the societal barriers applying to women attempting to obtain consumer credit apply to commercial credit as well.

Because market processes were not leading to automatic improvement of the credit situation for women, and there was no automatic tendency for the economy to lead to improvement, assuring improvement in the future required a sociopolitical intervention.(60) In the early 1970s the intervention came in the form of the Equal Credit Opportunity Act as a response to the pressure of women to correct unfair credit practices.

The Equal Credit Opportunity Act, which became effective in October 1975, provides that it is unlawful for any creditor to discriminate against any applicant for credit on the basis of sex or marital status. The law covers all aspects of the credit transaction. The intent of the law is that sex is not relevant to risk determination, and that archaic and sex-stereotyped considerations which have nothing to do with a woman's willingness and ability to repay a debt, can no longer determine whether or not the credit is to be granted. Business credit was included in the law. Regulation B, promulgated by the Federal Reserve Board, implements the law. There is, however, a difference between the law and the regulation, and Regulation B exempts banks from certain requirements of the regulation when extending business credit. For example, business credit is exempted from the notification requirements regarding an applicant's rights, the limited prohibition against inquiry as to marital status, and the automatic maintenance of records, although records must be kept upon written request. Specific reasons in writing for rejection of the credit request must be given by the bank, but only upon written request from the potential borrower. The effective impact of the procedural limitations is that women seeking business credit are virtually excluded from Regulation B's protection. Importantly, however, the law and regulations prohibit the use of attitudes about women that are derived from socialization processes in making business credit decisions. For example, questions as to the applicant's private life and family planning are prohibited. A creditor may not discriminate against an enterprise on the grounds that it is owned or operated by a woman but must consider the quality and capability of the enterprise's management and judgments must be based on sound credit criteria, the same as those which are applied to men.(61)

The Study Team found that the impact of ECOA on credit practices of commercial financial institutions has not been great. (Our findings are described later in this chapter.) Despite the limitations of the regulations, the uneven application of the law, and the slow enforcement process, the Equal Credit Opportunity Act yet may become a major step in reducing societal barriers to the acquisition of credit necessary to business ownership. However, because the remaining problem is more one of *de facto* rather than *de jure* discrimination, the solution is more complicated than merely passing more laws.(62)

Because there are no uniform requirements for commercial loan packages, at the moment it would be very difficult to monitor Equal Credit Opportunity Act compliance in the area of commercial credit on any basis other than that of investigation of individual complaints. Thus far there have been few complaints filed. Increased effectiveness can occur only after a system has been established to monitor compliance industry-wide.

We recommend, therefore, that a study be done looking to the design of a reasonable and feasible monitoring system of Equal Credit Opportunity Act compliance for business credit. *Included in this study should be an evaluation of the criteria for determining credit worthiness to determine their validity when applied to women*.

We also recommend that the Board of Governors of the Federal Reserve System amend Regulation B to read that all individuals applying for business credit be told specifically and clearly their rights under the Equal Credit Opportunity Act. In order to relieve any potential paperwork burden we suggest that the agencies regulating financial institutions distribute pamphlets stating the borrowers' rights and the creditors' obligations under the law.

Women's Banks

Lack of credit contributes to the economically disadvantaged status of women. One response to the effort to end credit discrimination against women was the expansion of a special type of financial institution controlled by women.(63) The first women's bank opened in 1919 and the first savings and loan in the 1920s. As of mid-1978, there were seven commercial banks, four savings and loans, and 17 credit unions.(64)

The major difference between women's financial institutions and all others is that they are committed to ending discrimination against women while serving the needs of all their customers, men and women. Women's banks have stated in their charter applications that they will give special attention to the credit needs of women--a community need and service the organizers feel has not been met in their respective communities. The women's banks provide personalized, individual attention to help allay women's fears that they will be considered ignorant, unsophisticated, or lacking in financial judgment when asking for a loan. The banks pride themselves on taking more time with women opening small businesses than traditional banks do.(65) Among the special services women's banks offer are seminars in starting a business.(66) In addition to loans, women's banks are developing trust departments and financial and investment counseling services which the organizers feel commercial banks do not now adequately provide.(67)

Women are in the banking business because of the profit motive; the banks are business-oriented and are not cause-oriented. Like other banks they are concerned with proving themselves by producing a reasonable return on equity.(68)

Only time will tell if the Equal Credit Opportunity Act has diminished the need for these institutions.(69) If ECOA is vigorously enforced, no bank will be able to discriminate against women and women may prefer the efficiency and wide range of services provided by bigger, more established banks. On the other hand, despite ECOA, a bank which women feel meets their special needs may well fill a vital need in many communities.(70)

The Treasury Study Team contacted the women's banks across the nation and found their managers very helpful in defining the relevant issues, such as the need for capital and credit by most small business owners, and the problems women have in obtaining credit.

Accessibility of Credit

If discrimination on the basis of marital status were operating in banking practices, we could expect that some categories of women business owners would receive less money than others when applying for the same size loan. To check whether this was true of the Task Force questionnaire sample group, the responses on the questions related to "size of loan sought" and "amount obtained" were converted to percentages so they would be comparable. Then the percent obtained was subtracted from the percent sought in each amount category (e.g., loans of $1,000 to $5,000).

If the women received what they applied for, that percent difference would be zero. If the amount requested minus the amount obtained is less than zero, we can infer that the loans granted were for less money than that requested (because more loans fall into the lower dollar category). If the difference is greater than zero, we can infer that the loan obtained was greater than the original amount requested. This kind of a check is extremely rough and small differences probably mean nothing. To draw conclusions we would have to use a random, stratified sample of participants and a far more rigorous statistical analysis of the data. Table 3 shows the outcome of these calculations.

Several inferences can be made from the pattern of differences.

-- Frequencies of zero or positive outcomes are as follows:

Divorced	11
Married	10
Widowed	8
Never Married	5
Separated	5

TABLE 3

Percent Differences: Loan Amount Requested Minus Loan Amount Obtained by Current Marital Status—Women Business Owners

Dollars in Thousands

	$1-5	$6-10	$11-15	$16-20	$21-25	$26-30	$31-40	$41-50	$51-75	$76-100	$101-150	$151-200	$201-500	$501-1,000	$1,000 or more
NEVER MARRIED (N = 173)	− 9.0	+ 9.6	− 4.8	− 0.5	+ 2.1	+ 3.5	− 0.6	0	− 1.4	− 0.3	X*	X*	− 0.3	X*	+ 0.6
MARRIED (N = 1,064)	− 3.0	+ 0.4	− 0.4	+ 1.2	− 0.1	+ 0.1	− 0.3	+ 0.6	+ 1.1	+ 0.3	+ 0.2	0	+ 0.2	0	0
DIVORCED (N = 363)	− 5.5	+ 2.4	+ 0.5	+ 1.2	− 1.2	+ 0.4	+ 0.4	+ 2.2	− 0.9	+ 0.1	0	+ 0.4	0	+ 0.3	− 0.1
SEPARATED (N = 42)	− 4.9	− 0.4	− 1.7	+ 1.2	+ 6.0	− 1.1	+ 1.2	+ 1.9	− 4.0	X*	− 2.4	X*	− 0.5	X*	X*
WIDOWED (N = 157)	− 3.7	+ 0.7	0	+ 2.2	+ 0.2	− 0.6	+ 0.9	+ 0.7	0	+ 0.3	− 0.4	+ 0.4	− 0.4	− 0.2	X*
COLUMN TOTAL (N = 1,799)	− 3.8	+ 1.6	− 0.5	+ 1.0	+ 0.1	+ 0.4	0	+ 0.8	+ 0.2	+ 0.2	0	+ 0.1	0	0	0

X* = no loans requested or received.

SOURCE: Task Force Questionnaire

Thus, there may be a difference in the way women are treated by lending institutions. Divorced and married women appear to be more successful than other marital categories in obtaining the funds they feel they need.

-- Although most of the loans are for relatively small amounts, some women have been successful in obtaining very large sums.

-- Smaller loan requests get reduced more often than larger requests.

Additional data from the questionnaire indicate that 69.7 percent of the loans were secured by collateral with a somewhat larger proportion of widowed and married women securing their loans than unmarried women (72 percent versus 60 to 65 percent).

Of those business owners who have, at some time, applied for bank credit and been turned down, separated women were turned down most often (49.0%), followed by divorced (48.9%), never married (44.7%), married (33.6%), and widowed (26.6%). The banks gave reasons for the turn-downs in at least 75 percent of the cases with "lack of collateral" the most often cited followed by "bank policy regarding small or new business owners" next most frequent.

We have mentioned that the bankers we interviewed feel certain educational experiences are essential to obtain a loan, however, without comparable data on male entrepreneurs we can make no conclusions about how uniformly this criterion is applied. Among our respondents semesters of business or math courses taken in high school appear to have little, if any, relationship to the size of loan obtained. Courses beyond high school also have little relationship to loan amount, as all categories of "number of courses taken" show approximately the same distribution across the loan amount categories. There is a difference in the numbers of women in each of the groups under "numbers of semesters of business or math courses" with 64.6 percent having taken three or more semesters of business or math courses in high school. Only 25.3 percent have taken three or more courses such as these beyond high school. There appears to be no uniform application of the educational criteria for women according to the data, since those respondents with more business-related education did not get more or bigger loans.

Business Owners and Commercial Banks

One of the most intriguing questions the Study Team asked lending officers was, "Do you recognize women as a viable sector of the entrepreneur market?" The response, loud and clear, was, "WHAT WOMEN?!?!" The findings seem to point to the conclusion that women business owners are certainly viable -- to the extent that they exist at all -- but they constitute so tiny a segment of the entrepreneur market as to be practically invisible. In seeking answers as to why this is the situation, and if sex discrimination in commercial banks' lending policies plays any role, the Study Team found some expected and some very unexpected answers.

The most frustrating aspect of assessing credit and capital formation as it relates to women business owners is the lack of information available. Recent legislation (ECOA) designed to eliminate sex discrimination in credit practices may have inadvertently obliterated data that might have shed light on this area. Bankers are confused. One banker said, "I don't know how to lend money to anyone anymore." Bankers feel damned if they do and damned if they don't have records indicating sex and racial designations.

In an effort to evaluate the current state of banks' relationships with their female commercial clients, the Study Team attempted a dual data gathering program consisting of (1) a series of roundtable discussions, and (2) interviews with bankers in commercial lending. Six cities representing regional banking centers were selected. They were Washington, Chicago, Atlanta, Dallas, Los Angeles, and New York. Washington, though not considered a major financial center, provided the Study Team a close-at-hand opportunity to test the data collection techniques of the interview guide and the roundtable format.

Banks of the type most likely to provide commercial financing were selected from those with deposits in excess of $100 million on the somewhat arbitrary assumption that smaller banks would be less likely to have made a large number of commercial loans to small businesses and would have fewer experienced loan officers specialized in commercial lending available for interviews. The shortness of time available for data gathering also influenced the decision to focus on banks not highly dispersed. In order to avoid concentration on the largest banks, selections were made from three categories: approximately 30 percent were in the $100 million to $250 million in assets range, 20 percent in the $300-$950 million range, and 50 percent in the over $1 billion category.

Though it was not possible in the time available, a survey of small town and non-branch suburban banks would help complete the picture. There appeared to be some indication from interviews that because very small banks know their customers better and are more in need of small business customers, women business owners may find a warmer welcome there than elsewhere. In contrast, however, the Small Business Administration indicates that most of their transactions are conducted with only 700 of the 15,000 banks throughout the country, and the majority of those banks are located in the areas visited by the Study Team.

Because the suggestion had been made that women bankers might have a significantly different viewpoint from their male colleagues, women bankers were asked to participate in roundtable discussions with women business owners. Other bankers, specifically commercial lending officers, both at the policy level, and those with large small-business loan portfolios, were asked to submit to in-depth, structured interviews conducted using a set of open- and closed-ended questions. A copy of the interview guide can be found in the Appendix.

While setting up the data collection process, we observed differing reactions among those asked to participate. Women bankers were approached through suggestions from the National Association of Bank Women and a sort of "old girl" network of referrals. They appeared extremely cooperative and eager to share their time and knowledge with the study group. They are justifiably proud of the strides they have made in the banking industry, eager to share their expertise and very cognizant of their high visibility. At the same time, women banking professionals, having gotten where they are by dint of hard effort, are extremely wary of easy answers for commercial customers who also just happen to be women. Some 67 women bankers, three men bankers, and many women business owners took part in the roundtable discussions held in the six cities. One additional roundtable of 10 minority women business owners was held in Washington.

Gaining the cooperation of lending officers, approached directly through phoning the banks, proved a more difficult task -- in all fairness, probably due in some measure to inadequate advance notice. Highly suspicious of the motives behind our data requests, and generally wary of "the Government" snooping into their lending practices, some 51 bankers knowledgeable about commercial lending agreed to be interviewed.

Of the bankers interviewed, 80 percent were male, 99 percent were non-minority, 80 percent were married and had an average of 2.8 children. They averaged 15.3 years of banking experience and nearly three-quarters of them had a college education or better. Three-fourths of the bankers in the survey were between 30 and 50 years of age. About two-thirds of them listed spouse's occupation as "housewife."

Mail Survey: The Task Force's questionnaire was used to obtain input from women as to their experiences and perceptions of commercial lending practices. Of the 2,913 women business owners who answered the questions "Were you one of the original founders of that business?" and "Have you ever applied for bank credit for the business?" we found that 64.8 percent (1,502) of the founders have applied for bank credit.

Founders were asked whether they started the business alone. Each response was then compared with the answer to the question "Have you ever applied for bank credit for this business and been turned down?" Of those women who started the business alone, 42.9 percent (309) have been turned down.

Other responses were as follows:

How Business Was Started	Percent Turned Down	Number Turned Down
Alone	42.9%	(309)
With Spouse	33.6	(206)
With Other Family Member	35.9	(42)
With Non-Family Member	39.5	(120)
With a Combination of Family and Non-Family Members	34.5	(30)

Several observations can be made about these data. (We must remember, however, the flaws in how the responses were obtained; for example, respondents were not randomly selected.)

- Although the percentage turned down is greatest for those who started alone, there is very little variance between categories.

- The average turn-down rate is 38.4 percent. This rate applies to all credit encounters over the life of business.

- The other side of the coin is that 61.6 percent (1,134) of the founders of these particular women-owned businesses HAVE NEVER BEEN TURNED DOWN WHEN THEY APPLIED FOR BANK CREDIT.

What, then, are the circumstances that portend a business owner's successful quest for commercial credit through ordinary banking channels? What are banks looking for in their commercial customers?

We found in conducting the interviews that almost everyone -- bankers and women business owners alike -- agrees that women are likely to own small service or retail sole proprietorships, which do not produce a hard product or a professional service. Almost universal agreement can also be found that commercial banks are not in the sort of business that can afford the extremely high risk involved in financing the "start up" of such enterprises. Nor can banks usually afford the high costs of administering many very small loans (less than $25,000) when the return for the time invested is much greater on a few large loans.

In assessing the banking industry's interaction with entrepreneurs, the discussion is, by definition, focused on on-going businesses with some track record of performance, some healthy assets, some demonstrated managerial expertise, and some very convincing reasons why a considerable amount of additional credit will enhance the prospects of the business. If lending "start-up" capital is anathema to bankers, lending "bail-out" capital is even less attractive.

The survey revealed that commercial loan categories vary widely, depending on the internal organization of each institution. Loans may be recorded by size, subject matter, by purpose, by collateral, or simply by geographical location. Borrowing requirements determine the location of the loan, i.e., branch or headquarters office. Almost all bankers interviewed indicated that their banks had no dollar amount cut-off for classifying a loan as being a "small business" loan. At the same time, the definition for a "small business" varied from hobby-type cottage industries to under $5 million in sales per year. Bankers generally feel bullish toward lending to well established, small or medium-sized business and indicated that economic downswings do not restrict money available to small businesses due to the relatively small amounts involved per customer and reduced borrowing demand on the part of large corporations. "Competition among banks for the large corporate accounts is very tough," one banker said. "In any event," another banker commented, "existing customers are serviced first when a tight money situation arises." Bankers were asked to estimate the percentage of small commercial loans made by their banks. Answers ranged from less than one percent to about five percent. Of that small percentage, most subjects interviewed could recall at least one female client, but most of their comments were similar to "very, very few," "can't remember the last one," "only a handful," or "some couples where the wife manages."

When bankers were asked why they thought more women did not apply, they frequently cited the social and cultural conditioning traditional for girls in our recent history. Comments included the following:

** Women who have earned good money, have worked to achieve and are hesitant to leave the known for the unknown -- they are not yet motivated.

** Opportunities are better in large businesses.

** This area of the country is not progressive -- it is way behind the East and West coasts.

** There is a need for education in financial management and accounting.

** Women lack confidence.

** Women don't read the financial press -- they don't understand money.

** Women are not electing to (enter business) at this time -- it will be very different in 10-20 years.

Bankers also frequently made comments regarding their perception of changes in the making. Examples:

** Women are now cutting their teeth in management and may soon be showing up as really good candidates.

** More women are applying for loans now that there are more corporate officers who are women.

** The gap between men and women in education, work experience and level of expectation is narrowing.

Some effort was made to ascertain any differences between male and female business owners' approaches to bank selection. While bankers usually felt that their calling programs and advertising were effective, they said referrals bring in most new customers of all kinds. While indicating that they thought both men and women had the same kind of referrals, bankers mentioned "husbands" and "family contacts" only when discussing women clients.

One question in the survey addressed itself to preliminary phone calls from women. Bankers did not seem to think more women made such calls than men, or asked any different questions as they "let their fingers do the walking" while shopping for banking services. If, as some roundtable participants suggested, women are more timid about walking into a bank and try phoning first, no survey evidence was found to indicate that banks are aware of such a possibility or take any special pains to allay such feminine fears. A recent author made the following observation:

> I know that most of us are or have been rather timid about approaching banks. There's a somber, forbidding atmosphere that often surrounds money in an institutional setting. A lot of this is a legacy of the past fifty years, when banks were deliberately built to look like money temples, their high-vaulted ceilings echoing and re-echoing like the nave in Westminster Abbey. Then there are those heartrending movies of the thirties on the Late Show, with the impoverished farmer sitting hangdog with his hands between his knees, at the mercy of the well-fed, well-dressed banker behind the big mahogany desk...(71)

Bankers uniformly indicated that no research had been done to detect male versus female pay-back rate differences. Some reported that they had no feeling for one way or the other. Others felt that the female pay-back rate was as good or better as that of men. Some seemed to regard it as a trick question.

Survey participants were asked to try to construct a profile of commercial applicants and comment on any differences they may have noticed between men and women. While no clear picture emerged, some of the most often mentioned characteristics for all applicants included: age in 30's, degree or some college education, some experience in the field, with risk-taking personalities. Bankers indicated that the few women they are seeing tend to be younger, better educated, more tenacious, and better prepared than the men. "They may have given it much, much more thought than men who assume they can just jump in." But women are still deemed deficient in "hands on" experience directly related to the venture they wish to undertake. "They usually worked in production or sales and have no financial experience and may be overly optimistic."

The kinds of business experience bankers are looking for varies a great deal from individual to individual. Some of their comments were: "It depends on the size of the the loan", "Minimum of three years", "Quality, not Quantity", "Depends on the industry, doesn't have to be specific, but should be transferable," "Purchased experience (from attorneys, accountants) can substitute", "Should be practical", and "Ten years in the industry, at least three of which should be managing a substantial line operation".

Among the reasons frequently mentioned as problems with loan requests and explanations given for turn downs, were the following, in approximate order of frequency mentioned:

- Inadequacy of preparation of proposal
- No prior business experience
- Company under-capitalized
- No money of own to invest
- Lacking accountant/attorney input
- Lack of market survey or projection of anticipated earnings

Bankers said they did not consider the lack of a credit record a major problem. They indicated that only a bad report would be a factor in a loan for business purposes.

Bankers were asked how much equity and collateral they looked for. Most of them indicated that it depends on the industry, but most frequently indicated was a two-to-one debt/worth ratio at the very least. Again, they reiterated that too little money on the part of the business owner is a big problem. Bankers complain that the new business owner wants the bank to put up all the money. For example one banker made the statement, "Women are not looking for a loan, they're looking for a partner." Some of their comments in response to "How much equity are you looking for?" included such responses as "125 percent," "as much as the bank is putting in," "decreases on the basis of track record and experience." Only one banker indicated any difference for women. He said, "Women may have to have more."

Bankers indicated that they had no commercial loan application per se. Rather, they depended on financial statements, letters outlining projects, copius notes, etc. Some of the things they mentioned looking for included personal resumes, financial projections, primary and secondary sources of repayment. Credit history was mentioned also -- although again the emphasis was on there not being something derogatory, rather than the extent of it. One banker mentioned "common sense" and another indicated he relied on "looking him in the eye," as parts of the process of gathering information about the prospective loan.

In response to questions about who has the authority to decline loans, most bankers indicated that while loan officers have authority to lend up to some specified limit, they can essentially decline much bigger loans by simply never bringing the application to the next higher authority. Although few bankers indicated having a committee for deciding to decline loans beyond the individual's lending authority, most banks seem to have a very informal arrangement consisting of checking with the credit supervisor or having two officers on a "turn down." Bankers did not seem to feel any discomfort with this system as sufficient to provide a check on possible individual prejudice or personality conflict. One banker said, "An early turn-down is sometimes kinder." One of the women bankers at a roundtable told of a women applicant for a $100,000 loan who didn't hear for two months if she was approved or not, and another commented that "maybe because she was a woman she would wait."

One survey question attempted to probe the mechanism of how banks assign loan applicants to loan officers. Methods for handling this vary a great deal in the banks surveyed. Some banks do have assignments made by management or simply by workload, but many banks seem to let the chips fall where they may. Bankers indicate that junior officers naturally cut their teeth on the smaller loans. Larger loans find their way to other officers experienced in the heavy servicing required by larger businesses. One banker said, "The secretaries screen for size -- bigger loans to vice presidents, smaller ones to assistant vice presidents." In branch banking situations, smaller commercial loans usually stay in the customer's own branch. As the size of the bank increases, so do the number of loan officers who specialize in certain industries, types of business, or SBA loans. Junior loan officers are on their own to drum up business for their loan portfolios through calling programs and working their own contacts. One banker commented that junior officers like to lend to new businesses. A successful new business customer is a long range prospect for the bank in general and for the loan officer in particular. One banker did mention personality and another compatibility as factors in assigning loan applicants.

The questions about assigning loan applicants were immediately followed by questions related to women loan officers in an effort to see if bankers felt women loan officers might have some different perceptions toward women in the highly subjective matter of sizing up an applicant. Even reminded of their comments about personalities and an individual's contacts, most bankers felt having female loan officers was not a high priority. Some comments were: "There are plenty of women out in the branches", "Some women like female loan officers, others don't recognize their expertise", "Not enough women applicants to try the idea", and "See no purpose". Other comments indicated an evolving new feeling about having women loan officers available to women applicants: "Not done now, but believe it would work", "(Women) might find it easier", "Sometimes a customer requests a black or a woman", "Useful from the standpoint of relating". Some banks indicate they are now experimenting with minority officers helping develop new business. One banker said, "It is very important for blacks ... not sure about females." Whether the blacks' situation parallels that of non-minority women in this area is not at all clear. The comments of some roundtable participants seem to suggest that non-minority women, especially in the South, move in the same social circles as bankers and can converse across a desk as easily as across a dinner table. There also is some indication that female loan officers are far from coddling their female applicants. One female loan officer at a roundtable said, "I think I'm probably tougher on other women than some of my male counterparts -- because I expect women to be more professional, just like I try to be. My male counterparts have each spent lots of time with two women clients that I probably wouldn't have spent the time with. They went out of their way to help these women."

Another commented, "We don't make any leg loans," referring to a woman's loan being facilitated through flirting or acting helpless.

When queried about the percentage of women loan officers in their banks, most subjects in the study had no idea unless there were so few that they could be counted on the fingers of one hand. Other answers ranged from none, up to about 20 percent, except on the West Coast where estimates were 40 to 50 percent. Some indicated that female branch managers counted as loan officers, too. Often bankers said that they had women in training programs for lending officer positions, but the percentages were quite small except in the Los Angeles survey, where up to 60 percent of lending officers in training are women. In Los Angeles, the training programs in some banks offer a specialization in small business commercial lending. A southern banker mentioned that he didn't think women were attracted to this area of banking because of the unpleasant factors, i.e., turning people down.

Near the end of the interviews, bankers were asked what they thought were the major obstacles to women trying to run a business or start a business. Many of their answers to this question were similar to answers to why more women did not apply for business loans. And while several bankers insisted the obstacles are the same for everyone, many indicated their sensitivity to women's special situation in getting into business and staying there. Some of the things they said were:

** Women don't have the temperment, they can't manage people, don't want the long hours.

** Women have to overcome the traditional bias against them.

** Women lack experience and the opportunity to get it -- comes from their non-breadwinner history.

** Women lack entrepreneural drive -- their competitive instinct may be missing.

** Women have had a non-business "up-bringing."

** Capital requirements to start a business are greater than in the past -- it is now harder to make "sweat-equity" result in success.

** Women are not usually free to consider business ownership as an option.

** "Contacts" are missing.

** Women don't know what they are getting into.

** Women face psychological barriers -- skepticism of women as entrepreneurs -- they need cultural support.

An effort was made to determine to what extent banks may now be courting prospective women customers through special programs or advertising. Responses were divided between those banks doing nothing (2/3) and those making efforts to attract women-owned business accounts (1/3). Some of the responses were as follows:

** We are trying to set up a women's department -- looking for someone to head it -- we are now exploring women as a market.

** We participate in local National Association of Women Business Owners seminars.

** We're thinking about it; not much money for it.

** No, but lending personnel are active on the speakers' circuit.

** No, but we do locate (branches) in shopping centers (where women are).

** We have special personal banking services.

The surveys and roundtables revealed that although little is now being done to attract women customers, some banks are beginning to explore the possibilities. Some ideas, such as a large mid-western bank's filmstrip and tape program, which are minority oriented, are being adapted to fit women. Most of the push to seek actively women customers appears to be coming from within the the ranks of professional banking women. In the roundtable sessions many women bank officers indicated that they made an effort to participate in speaker's programs for women's organizations and school-connected programs at many levels, including the highly-regarded Junior Achievement Program at the high school level. These women appear to form the backbone of educational efforts now underway to help women become more knowledgeable and more independent in their financial dealings.

The study team asked bankers about the Equal Credit Opportunity Act. First, they were asked what effect they foresaw on their approach to the small business community if the record keeping requirements were extended to include commercial loans. Despite considerable groaning and sighing at the mention of ECOA, responses proved to be rather mild. Some typical responses:

** Impact would be smaller in the commercial area because of fewer people.

** Confident of (positive) effect on the consumer credit score, not sure there would be an effect on commercial.

** Would change procedure, but not really availability.

** Only affects paperwork.

** Administrative nightmare, doesn't make more credit available, but is consciousness-raising.

The more negative responses indicated a fear that the cumbersome compliance paperwork added to the cost to the customer, made it tougher to get credit, and took away valuable counseling time from the very customers who needed it most.

In zeroing in on Regulation B, bankers were asked what might be done to make operations easier without changing the intent of the law. Frustration at the paperwork problem seemed to be universal. Everyone hates it. One banker indicated he simply refuses to deal with it and relies on "someone else to keep him out of trouble." After availing themselves of the rare opportunity to "sound off" about Regulation B to someone from Washington, many bankers conceded that even though it may have been a case of overkill, they "agreed with its purpose" -- that "there probably was a need for some push," "it made everyone aware of abuses," and "may be necessary because intent to discriminate is hard to find."

In considering the extension of ECOA requirements to the commercial area, bankers fear losing that "free exchange" with their customers that they feel they now enjoy. They feel that having mandatory reporting requirements are unnecessary because they are complying with the intent of the legislation. Figures from the Task Force Questionnaire sent to women business owners seems to support the bankers' contentions. Some 82.4 percent of business owners reported being told the reason for their being turned down for a loan.

In trying to come to grips with the implications of all that bankers told the Study Team, one key factor emerges: women must understand that "equal credit" does not mean "easy credit." In many instances, the stories related by women entrepreneurs alleging discriminatory credit practices could be examples of banks applying their "standard" credit criteria, i.e., estimation of the applicant's ability to repay and intent to repay. For example, consultants must collateralize loans with something harder than a signed contract since there is no guarantee, as far as the bank is concerned, of performance on the part of the consultant. Women must come to the understanding that banks are in business to make a profit -- not for any social reason. Women must understand that often it is against the high-risk nature of small business undertakings that banks are prejudiced -- not against women as a class.

If women are able to originate a viable business enterprise through private or some other source of capital, then the question of prejudice in obtaining loans from commercial banks is another matter. Because the credit judgment is a highly subjective one, it is quite possible that a male applicant would be judged more credit-worthy and that less collateral would be required for his loan. Of course, this discrimination is the most difficult to substantiate and will be the most difficult to overcome.

The data on discrimination complaints are very scanty. Some technical violations have been found, but virtually no substantive complaints have been filed. While numbers of complaints may be related to degree of education with regard to legal rights under the ECOA, no studies have been done to substantiate such a premise.

The Study Team feels that written notification of adverse action would not be the best way of educating women. We believe that if there is discrimination against women business owners it occurs long before a loan request is declined--it occurs when the woman telephones for preliminary information, or it occurs before a complete loan package is formally submitted. Women need to be informed of their rights during the preliminary negotiations with lending institutions--that is the point at which they are precluded from entry into the system. What must also be stressed is that women do not now possess the qualifications men do to meet banks' lending criteria. This means that attempting to compare male and female applications would be very difficult, for not only does the woman's personal qualifications have to be comparable, but her business' characteristics must also be comparable.

Comparison would be further complicated by the fact that a banking decision made today can be validly compared only with another decision made under the same circumstances. We are all familiar with how interest rates fluctuate and the impact changes in rates have on fund availability for small loans. What this may mean is that saving records for two years or ten years would not matter. Saving records would mean that greater numbers of female applicants could be captured, but they would not necessarily be comparable. In addition, for every application from a woman, approximately 999 applications from men would have to be stored.

In discussing records, one more point must be made. Consumer credit applications are pretty much standardized (due to Regulation B) and are one page of information. Credit worthiness is judged by an actuarial-type of method of awarding points for different characteristics such as income, number of years on the job, home ownership, etc. Business credit transactions are far more subjective. There are no formal loan application forms, usually a loan package is built from financial statements and resumes from the principals, financial statement or profit and loss statement for the business, cash flow projections and five-year business plans, marketing analysis, etc.

Before we can require banks to comply with new regulations, we have to first define what it is we are talking about. Before we can require that "records" be retained, we have to determine precisely what information would be needed to seek judicial remedies for a discrimination complaint. We need to develop the framework for a viable compliance monitoring system <u>before</u> we can require banks to change their operations and incur additional costs. The Task Force should press for the development of a system that will work, based on sound principals of both social science and law. Merely extending provisions of a regulation designed for an entirely different kind of transaction is not in the best interests of the woman business owner.

In analyzing the written materials and the data collected in the field study, the Study Team can state only that our findings are inconclusive. Little or no direct evidence was found that women have unique problems in obtaining business credit, <u>all other things being equal</u>. If women are not presenting loan proposals which are as strong as men's, that is not the fault of the banks. The barriers to women which prevent them from successfully approaching banks are constructed long before the loan is applied for.

They are built when a woman decides on a course of study, when she plans her career to exclude substantive work and management experiences, and when she neglects building a capital base to support her desire to own a business.

In short, women who wish to eventually become entrepreneurs must get into the "pipeline" early on; and this is exactly what they are now doing today in large numbers -- whether they know it or not.

Commercial Banks and the Small Business Administration

If a business is able to stay in business and make a profit for several years, it experiences a natural tendency to expand and grow. It is at this point that businesses that have done well in the past suddenly fail, often because of extreme cash flow problems. Sometimes the failure is a consequence of management inadequacies. Problems which could be finessed in the small enterprise can become overpowering in the rapidly growing business. A roundtable participant said, "In your report please put in something about helping those women business owners who are already started -- at least that have a track record...Help! Help! Help! We're in over our heads now. What we were able to do on energy, guts, stupidity and naivete, because we didn't know what we were getting into five years ago, is now at a point where it is critical for us to get some good, sophisticated help."

One source of financial and management/technical assistance for women business owners is the Small Business Administration. During our survey we solicited comments from the commercial banking community and from women entrepreneurs vis-a-vis their relationships with the SBA, turn-around-time on applications, the burdens of paperwork, how many loans under the respective programs were made to women, what percentage that was of their entire commercial loan portfolio, the dollar amount of the loan, if there were any particular difficulties with women applicants, and the primary reasons for loan default.

Analysis of the responses and voluntary comments did not reveal a bias in any particular geographical region. Further, it did not reveal any common experience and/or difficulty relative to the size of the bank surveyed.

The analysis did reveal three high priority areas of concern to bankers and women business owners. In order of frequency mentioned they are:

** increase the quality of management/technical assistance available (from the Small Business Administration <u>or elsewhere</u>);

** increase direct loan assistance from SBA rather than loan guarantees; and

** streamline paperwork required by SBA.

Time and time again was echoed a desperate need for management and technical assistance. The comment was made that because of the lack of management and technical assistance, people were experiencing business bankruptcy, loss of home and personal possessions, ruined lives. The bankers felt that weak management is the overwhelming reason why the majority of SBA loans fail. Bankers and entrepreneurs alike questioned whether a Federal agency should provide access to money either on a direct disbursement or guarantee basis without providing proper screening of applicants and access to adequate management and technical assistance. Responses to the field inquiries were used to develop a series of questions about the SBA Management Assistance Program, the answers to which were obtained from SBA headquarters staff.

<u>QUESTION</u>: What is the follow-through from the loan assistance stage to management/technical assistance? What is the average servicing caseload portfolio for a loan management employee?

<u>ANSWER</u>: A portfolio management loan officer conducts an initial field visit shortly after disbursement to check the use of loan proceeds and other conditions of the loan authorization. At that time, a referral is often made to the management assistance officer in order to provide management and technical assistance to the borrower. The average number of loans in a portfolio is 146.

<u>QUESTION</u>: Is the management/technical assistance personnel adequate vis-a-vis the workload?

<u>ANSWER</u>: No. The SBA is painfully aware of the shortage of qualified personnel. This has been a problem since 1968; we need four times

the present number of professional staff and those people should have varied experience to offer credible, sensitive assistance to fledging entrepreneurs. However, we do have the authority to utilize the private sector to provide this assistance and we do so through training programs which are co-sponsored with universities, community colleges, associations, chambers of commerce and, our 406 Call Contracting Program. This latter program, section 406 technical assistance, is available only to "socially and economically disadvantaged people." The Small Business Institute Program provides counseling from various business schools, often using their graduate students. In addition, counseling is provided by the Service Core of Retired Executives (SCORE) and the Active Core of Executives (ACE). All resources are managed by the management assistance office.

In our field study we often heard criticism of the calibre of management and technical expertise available from SBA. It appears, however, that the problem may simply be one of a lack of small business management experience among the counselors. Many of those employed by SBA are students with no experience or managers from large corporations. The Study Team was unable to verify this information given the short period of time available. We submit, however, that the heavy workload in many SBA offices is totally unrealistic and support SBA's request for Congressional assistance in the areas of budgetary requests and for the Civil Service Commission's swift cooperation in obtaining the needed personnel to meet the needs of the small business owner.

The second most frequent comment stressed the need for more SBA direct loan assistance. Following prudent banking guidelines, bankers commented, "If you have to rely on a guarantor to support a loan--it's a bad credit risk." Other comments: "If you've got a good loan, you can fund it directly. If not, it shouldn't be funded at all. SBA should make more direct loans." "The spread [profit] is too low for SBA guaranteed loans under $50,000. If there's no profit, why should the bank make the loan." "SBA guaranteed loans tie up our money for too long at too low a profit." "Turn-around-time on an SBA loan application can take anywhere from one to three and sometimes even nine months. This causes two problems for the business owners. One, business owners shop banks which means that if we can't respond, we loose a potential client. And second, small businesses cannot survive their cash flow demands when the turn-around-time is that unreasonable."

The Small Business Administration does make available direct loan assistance to those eligible applicants who have been denied assistance by two commercial banks. The obvious implication here is that the SBA does make available direct loan assistance to very risky transactions. If the SBA makes available more direct loan assistance the cost of this assistance will be passed on to the taxpayer. It should also be noted that utilization of the SBA's guaranteed loan assistance program is voluntary for the commercial banks. If a commercial bank finds itself in the position of not being able to assist a client with a business loan, it does have the option of submitting the loan package to the SBA for loan guarantee assistance. The SBA can provide the commercial bank with up to a 90 percent guarantee on the transaction and extend terms, *i.e.*, where the commercial banks would normally offer 3 to 5 years, the SBA guarantee loan assistance would offer 5 to 7 years for repayment. This does tie up the bank's funds for a longer period of time. However, there is a secondary market for guaranteed loans. This program has been in existence for five years and provides the lender with the opportunity to sell the guaranteed portion of the loan. The spread between the interest to be earned on the loan and its selling price is retained by the banks as a servicing fee. This allows the bank to increase its yield on the unguaranteed part of the loan that the bank retains in its own portfolio.

We asked the Small Business Administration a series of questions about constraints which would affect their ability to (1) hire qualified personnel to serve the public in a timely manner, (2) conceive of and implement new programs, and (3) generate internal statistics on their clientele.

QUESTION: What is the average turn-around-time for a response, either affirmative or negative, in each of SBA's programs?

ANSWER: After receipt of a complete application from an applicant for a direct loan, or a bank for a guaranteed loan (business type), the SBA response is 19 calendar days on the average. This varies by region and by district office, depending on the volume of applications at any given time. After approval, loan closing time may be considerably longer, depending primarily on the ability of the borrower to meet the terms and conditions of a loan authorization.

We hope to significantly reduce this time with new automated procedures.

<u>QUESTION</u>: Assuming a commercial bank is involved in a loan assistance request, with whom does SBA communicate, the enterpreneur or the financial institution? Please explain the procedure. Does this vary by region or office?

<u>ANSWER</u>: Assuming a commercial bank is involved, SBA normally deals with the bank, rather than the applicant. By law we cannot make a loan if a bank will make it without our participation; nor can we make a direct loan if a guaranteed loan is available. For these reasons all direct loan applicants must first be turned down by a bank (two, in cities of 200,000 population or more). This is the same in all SBA offices.

<u>QUESTION</u>: If a request for loan assistance is approved, what is follow-up procedure to monitor the loan? What is the bank's role?

<u>ANSWER</u>: Direct loans are monitored by the SBA Portfolio Management Division. Guaranteed loans are <u>primarily the responsibility of the bank servicing the loan</u> which also provides SBA with major decisions requiring concurrence of SBA.

<u>QUESTION</u>: Is a tickler file set up and kept current for each loan account?

<u>ANSWER</u>: We no longer have loan account tickler files as a national requirement; some field offices may use some form of Kardex or similar system. We are currently automating a monitoring system.

<u>QUESTION</u>: If the entrepreneur experiences operational difficulties which result in cash flow problems, <u>e.g.</u>, inability to make loan payments, what usually happens--does the entrepreneur advise SBA of the situation and seek assistance--or does a default occur? If a default occurs, what is SBA's procedure?

<u>ANSWER</u>: Rarely do we get an indication of trouble before there is a serious erosion of assets.

> <u>We rely on banks a great deal to monitor the accounts</u>, since we have 200,000 clients and only 4,000 employees. The system is not satisfactory. We recently requested that our budget be increased to include 1,200 new employees. We received 120, 60 of which are earmarked for the 8A program.

The Study Team also asked the SBA if they could generate data on respective program utilization by women business owners by geographic region. The response was that the SBA could generate data on loans given to women by region, but not on loans given to particular women-owned businesses. That is, they keep track of numbers of loan units to women but cannot generate the demographic and industrial data to complement this information. The SBA has only been generating data on women-owned businesses by race since 1974.

In Fiscal Year 1976, eleven percent (13,537 out of 118,413) of those counseled by SBA's management assistance staff were women. In the same year, 49,516 women out of a population of 183,630 SBA trainees were women -- over 27 percent. SBA had no data on procurement assistance given to women-owned businesses, although they are currently developing this capacity.

Another pertinent question posed to both the commercial bankers and to the Small Business Administration related to the percentage of defaults on loans to women-owned businesses delineating the type of assistance, date of approval, terms authorized, date of first disbursement, first due date, and date paid. The commercial banking community's management information systems were not able to report that information. The SBA could generate some of the information requested, however, the critical factors that would evidence prompt payment or the circumstances of default could not be readily generated. Thus, the Study Team did not press for this information, since the SBA appears to be making a herculean effort to improve their data retrieval capabilities.

Several recommendations for action can be concluded from this three-way dialogue:

(1) The Small Business Administration's management information system needs to be expanded to service its clients in a timely manner.

(2) The SBA should implement their pilot Bank Discretionary Program within the Loan Guarantee Program. This program should

improve communication and service between the SBA and commercial banks. The SBA should certify banks to make SBA guaranteed loans of no more than a specific amount without prior SBA approval and banks should be given greater authority to administer SBA loans, particularly with respect to the waiver of loan covenants.

(3) A bank that has made a loan to a small business without SBA participation should be allowed to roll-over that loan into an SBA guaranteed loan. This would ameliorate the current situation where a bank, after granting a small business a non-SBA loan, must refer the small business to another bank if it seeks an SBA guaranteed loan.

(4) The SBA direct loan program should be increased to aid women who cannot compete equally in the open market on the basis of "credit-worthiness." Concurrently, a test program should be developed and implemented to evaluate the validity of criteria used to judge credit-worthiness. Different probabilities of success could then be predicted on the basis of the different levels and combinations of experience, education, and capital available. This could result in a credit scoring system similar to those used for consumer credit.

(5) SBA should provide management training for women with a longitudinal study of outcomes as part of the program to evaluate results.

(6) SBA should institute standard, objective criteria for evaluating loan packages to limit regional subjectivity.

One of the criteria should be that applicants provide evidence of minimum level of experience and/or education in specific areas (such as accounting, financial management) <u>before becoming eligible for Federal funds or guarantees</u>.

Factoring and Finance Companies

Are women participating to a reasonable extent in this country's money markets? We have concluded that women are excluded, for a variety of reasons, from important financing sources. Two such sources which we suggest need attention are the use by women of finance companies and factoring institutions. Both of these financial institutions are associated with the on-going firm, and thus fall into the category of solutions for problems that women business owners meet after they have been in business for some time.

These problems are often associated with a need for short-term financing, which can arise from several causes: (1) the business is so successful that it cannot expand rapidly enough to meet demand, it cannot generate sufficient cash to pay for increased variable costs, and it runs into cash flow problems, and (2) the business is experiencing financial difficulties due to insufficient sales and is in danger of failing. The fact that it is almost impossible to locate data on the use of these two methods of bridging short-term money needs by women is a serious indication that women are failing to use fully all financing vehicles.

Factoring Companies: There are thirty-five major factoring companies both independent and captive in the United States, 80 percent of which are located in New York with the majority of the others in large metropolitan areas (Chicago, Dallas, Ft. Worth, Atlanta). When we called these companies not one could think of more than one woman client who was a full owner of a business. (It is true that a small number of businesses are jointly owned but the male partner deals with the factoring company.) This is even more surprising when the nature of the factoring business is considered. More than 80 percent of factoring clients are in apparel, an industry traditionally associated with a large number of women retailers. A majority of other important factoring areas are also in related "soft" industries such as carpeting, textiles and furniture while an even smaller segment deals with electronics and toy firms. What we are seeing, then, is a field in which women play a role at the retail level but have failed to penetrate to the wholesale, manufacturing or distributing level.

Factoring companies offer many services which could be of value to women business owners. By selling her accounts receivable to a factoring company she could pass on the chore of credit checking, with its additional cost of creating a credit department. Factoring companies would also absorb a major portion of her financial risk -- the collecting of accounts due. Many factoring companies offer related services that would be of enormous value to a vigorous firm -- the use of their computer for calculating sales commissions and the breakdown of sales by territory or sales person, the making of trade surveys, the finding of agents here and overseas, the compiling of management reports, and general business counseling are all services which may be offered by a factoring company.

Factoring could provide the woman business owner with liquidity and flexibility. Because of computer technology and the concurrent centralizing of credit functions, rapid increases in the factoring business are forecast. One large factoring company, for example, stated that its annual goal had realistically been set at a 10 percent increase on a current volume of $1.75 billion. Why, then, aren't women availing themselves of this important source of financing?

-- Women do not own many businesses in the manufacturing, wholesale, or distribution areas, those which factoring companies service.

-- Of the women in these fields, few own businesses of the magnitude necessary to be an attractive client. Most factoring companies insist on a business volume of at least $1,000,000 with a net worth in excess of $150,000. (Retailers may only generate a volume of $200,000 annually.)

-- Women are not educated to the use of factoring firms. Factors rarely advertise except at meetings of trade associations such as those in the garment industry, or in industry specific publications such as Women's Wear Daily or the Daily News Record.

-- Most factoring clients are referrals. They come to the factor through CPAs, lawyers, and above all, commercial banks. Women have traditionally not been part of this network.

-- The Small Business Administration, where many women go for advice and loans, decides on a case-by-case basis whether to allow owners to use factoring for expansion funds.

-- The criteria used to assess financing requests are the very ones women have traditionally found so difficult to obtain. As one vice president of a factoring company summed it up, "Track record, number of years in the business, qualifications, contacts, and personal references. That's all we look at, and all we need to look at. They tell the story." For a woman, these can create an insurmountable barrier.

-- In order to be considered as a potential factoring client a woman must be able to produce complete financial documentation on her firm which may create another barrier. Many factoring companies insist on a certain in-house format for balance sheets, operating statements, and sales forecasts. This may simply be beyond the skill or the financial resources of a woman who is facing a critical need for short-term financing. Few factors offer to do the work using their own accountants, and, naturally, would expect to be paid for this additional service.

-- Women often lack the necessary collateral to secure a factoring agreement. Rarely are personal assets accepted, although, occasionally, listed securities are approved. Generally, however, 80 percent of the accounts receivable is the maximum a factor will lend. This may create a "Catch-22" situation for the firm which badly needs funds to create sales to generate accounts receivable.

Finance Companies: Within the area of commercial finance companies the problems are much the same. Again, their function is to bridge short-term financial needs, and again we find very few women taking advantage of this form of financing. There are 130 members of the National Commercial Financial Conference, the finance companies' trade association, ranging from local to large national institutions. The managers we contacted insisted that women are "treated just the same as men," but then admit they have never had a woman customer, except as a second partner in a husband-wife-owned business. Commercial finance companies also sell to wholesalers, distributors, and manufacturers, all areas in which "women don't have any interest," according to one field sales representative. "Women," he added, "don't sell to other companies, they are mainly selling to the general public."

Barriers to effective use of finance companies by women include:

-- Misconceptions of finance companies due to insufficient education about money markets. Just as factoring firms traditionally have had the reputation as institutions of last resort for bankrupt securities, finance companies may be perceived as exorbitantly priced, last-ditch aids to a failing business. Confusion exists between the high rates they charge -- frequently 6-1/4 percent above prime, or about 14-1/4 percent today -- and the actual cost of their money. Finance companies can enable a client to get on a discount basis with a supplier (not a service provided by commercial banks) which may lower costs two percent, and can offer a revolving payout schedule with charges computed on an average daily balance rather than on the full term amount as is done with a commercial bank loan. All of these services significantly lower the actual finance costs.

-- Women are not perceived as a significant market segment and little advertising reaches them. Most clients are referrals from banks (which women may not even get into), whose officers suggest that a client go to a finance company after he has used up his line of credit.

-- Women have difficulty in meeting the collateral requirements from finance companies. Most of these institutions, if lending on fixed assets, will only loan 75 percent of the "knock-down value," i.e., the value they would receive if the business had to be auctioned off immediately. Most women are not in the position of owning large amounts of fixed assets.

-- Women do not frequently need loans in the large amounts finance companies prefer to deal with ($50,000 minimum loan for a very small finance company; a minimum of $100,000 or $200,000 is not uncommon for one of the larger ones). It simply is not worth their while to service small loans.

Thus, women may find themselves in the anomalous situation of being unable to find a company that is willing to give them the small loan they wish, because of diseconomies of scale, but of failing on the other hand to have the assets -- be they plant, equipment, or inventory -- to qualify for a larger loan.

Our survey of the field has turned up very few encouraging signals of a change in this trend. One large finance and factoring company in Chicago did have one woman client, in specialized manufacturing, who was buying out her boss's company with the help of $1,000,000 in funding guaranteed by her employer; hardly a typical situation.

When factoring and finance companies were asked if they made any attempt to encourage women business owners or perceived them as a separate marketing target, the answer was 100 percent negative. One field sales representative did mention having once attempted to solicit business from women using a metropolitan directory of women business owners compiled by OMBE.

Perhaps it is in this area that maximum effort should be applied. Making institutions aware of women business owners as a separate segment, educating and publicizing through the use of such tools as directories may be an important and reasonable step towards bringing women into the financial mainstream.

Other areas that also deserve consideration are: educating women business owners to the possibilities of using financing companies and factors by such means as lists of companies (perhaps categorized by size of loans offered) and their services and costs; facilitating obtaining SBA's permission for its small business owners to factor their accounts receivable would, in conjunction with increasing the number of SBA loans to women, offer another channel; encouragement, by whatever means, of women officers in lending institutions would further emphasize that sex plays no role in discouraging women from obtaining funds. Only when steps such as these are taken will there be significant use by women of these financial resources.

5 THE SMALL BUSINESS AND TAXATION

At present, there is no definition of small business in the Internal Revenue Code. A business is defined in the Tax Guides as a pursuit carried on for a livelihood or for profit; the profit motive must be present and some type of economic activity must be involved. Two characteristic elements of a business are regularity of activities and production of income. Business activities that result in a profit make the enterprise liable for taxes.(72)

The tax code is not the only place where it has been difficult to define small business. Lack of definition has impacted upon scholarly economic studies and analysis of the magnitude of small business in the economy.(73) Why is it so difficult to define small business in a clear cut way so that special tax programs can be designed to assist small businesses without increasing inequities in the tax system?

Small businesses can be categorized on the basis of receipts, employment, total assets, share of the market, income and value added. Value added is considered by many tax economists to be the best method of measuring a small business, but this information is not on the tax forms. Use of assets is another good method. However, it exaggerates financial institutions over other forms of business. Number of employees is deceptive because many businesses that make a great impact on our gross national product have few employees. Use of employees as a guide skews the definition in favor of labor intensive rather than capital intensive industries. Measuring small business by receipts has drawbacks as well, as receipts are not a good measure of the contributions of a firm to gross national product. Receipts also bias statistics in favor of those who buy and sell rather than those who manufacture a product.(74)

Use of income is very deceptive although Federal taxes are based upon income. In fact, many argue that income is the poorest of measures. Taxable income as defined in the Internal Revenue Code differs substantially from economic income and, because of special statutory deductions, surtax exemptions, alternative tax rates on capital gains, tax credits, and other special provisions, the apparent effective rates on income of businesses may vary substantially among industries and sizes of firms in any year. Use of income is further complicated by the fact that very large corporations may have low taxable incomes.(75)

Beyond general observations, such as that small businesses are clustered at the lower end of all these classes, exact statements about small business are hard to make. The basic difficulty is that there is no real reason to lump all small businesses together and no clear criteria for classifying them by size. We found no standard definition during our bank interviews, and thus the interpretation of what is small business is left to the interpreter.(76)

Taxation issues play a key role in defining barriers to the establishment of successful small businesses, primarily through their effect on equity infusion. The major sources of equity capital for expansion of a business are retained earnings and reinvested profits. The size of the total tax bite is an important determinant of the amount of money available for expansion. Of course, <u>taxation is not sex-specific</u>. <u>A small business is taxed as a business, not as female versus male-owned</u>. As a consequence, any changes in tax laws to benefit small businesses would benefit men more than women, since so few businesses are owned by women. Later in this report, when tax policies related to increasing the amount of venture capital are addressed, we will see that men would, again, be the major beneficiaries because so few women have sufficient capital to make such investments.

Forms of Organization and Type of Business

All businesses are not taxed at the same rate. Type of business, form of organization, and size of business are the major parameters defining total taxes owed. There are three different legal forms of business organization: proprietorships, partnerships, and corporations. Within each type of organization, nearly all types of businesses, from services such as travel agencies to heavy manufacturing, can be found.

The Task Force Questionnaire responses indicate that, among the community of established businesswomen, today's picture of legal form of ownership is quite different from what was represented in the 1972 Commerce Department study. Corporations, which were included in the 1972 study only if shown on individual income tax returns (i.e., Subchapter S corporations) represent 25.3 percent of our sample (as opposed to 0.3 percent in the 1972 study).

Table 4 shows a difference between the two groups of women with minorities forming more sole proprietorships and fewer corporations. On the question of how the business was formed, whether alone or with some other person(s), there was very little difference between the two groups, less than four percentage points in each category. These data indicate that 72.7 percent of the businesses were established by the woman alone (42.9 percent) or with her spouse (29.8 percent).

Gross receipts of the business in 1977 were also similar (see Table 5).

Minority women-owned businesses cluster at the lower income end to a greater extent with 58.5 percent making less than $50,000 gross in contrast to 45.1 percent for non-minority businesses. Of greater interest is the number of businesses at the upper end of the scale. Clearly, there are some substantial women-owned businesses in the sample. This fact is borne out by employment figures supplied by questionnaire respondents. Almost 30 percent of the businesses employ five or more people, 43.1 percent employ one to four people. Only 29 percent have no employees.(77)

The tax implications of each form of organization will be discussed in the following pages, as well as implications of tax policy on venture capital investment.

<u>SOLE PROPIETORSHIPS</u>: An individual engaging in business on his or her own account is a sole proprietor. Sole proprietorships are the simplest form of business organization. They have no existence apart from the owner, and the liabilities and assets of the business are the personal liabilities and assets of the owner. The proprietor undertakes all the risks of doing business.(78) Over seventy percent of all small firms are sole proprietorships. This form of organization accounted for 98 percent of the businesses and 89 percent of the gross receipts for all women-owned firms reported in the 1972 survey.(79) As can be seen in Chart 2 the dominant type of business for sole proprietorships is retail trade.

TABLE 4

Percent of Responses To Legal Form of Business Ownership: Minority and Non-Minority Women

	Sole Proprietor-ship	Joint Proprietor-ship	Partner-ship	Corporation*	Other
Minority Women (N=448)	57.8%	8.7	10.9	20.3	2.2
Non-minority Women (N=2504)	47.7	8.8	14.2	26.2	3.0
Column Total	49.3	8.8	13.7	25.3	2.9

* Including those who are substantial but not majority stockholders.

SOURCE: Task Force Questionnaire

Table 5

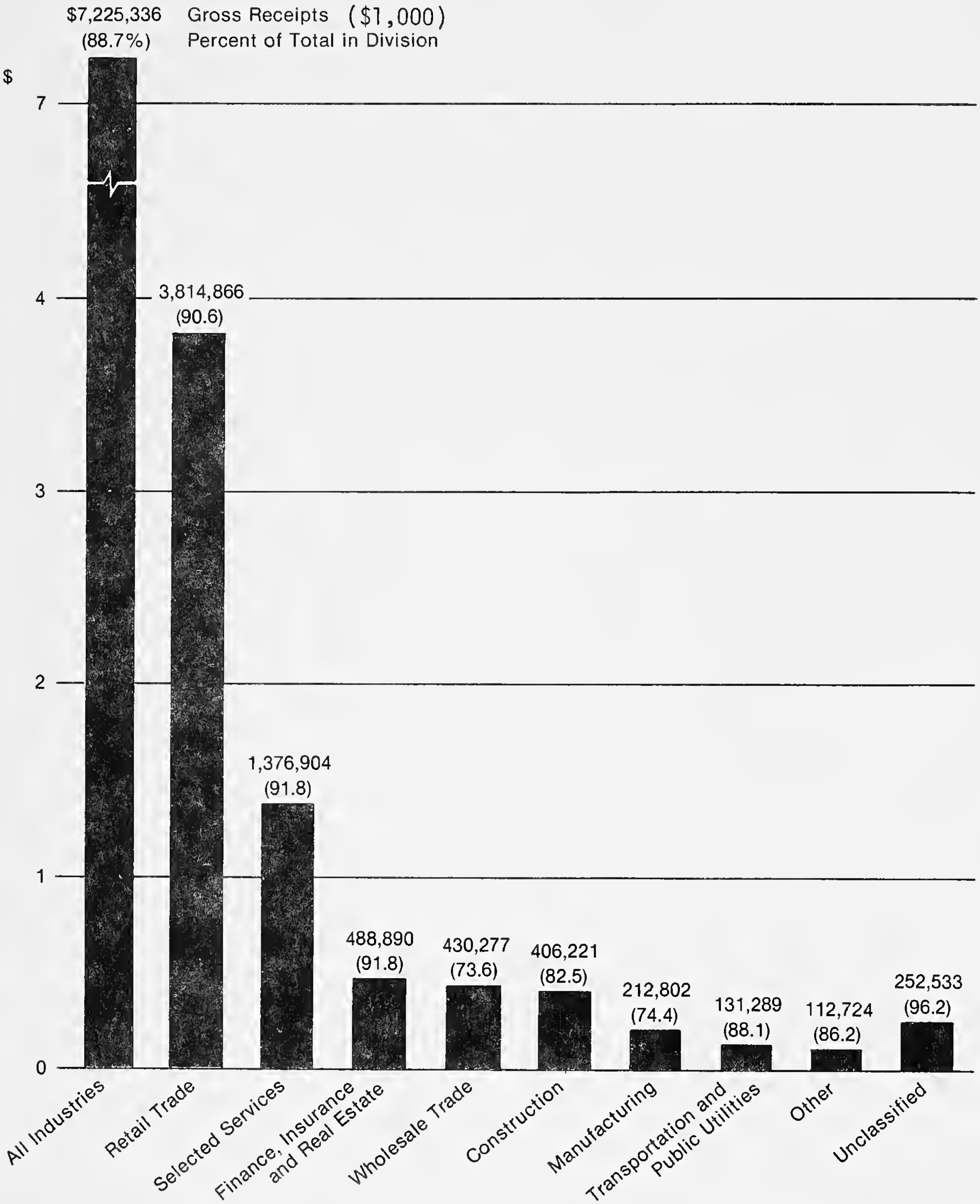
Percent Distribution of Gross Receipts - 1977 for Firms Owned by Minority and Non-Minority Women

	Under $10,000	$10,000 to 49,000	$50,000 to 99,999	$100,000 to 499,999	$500,000 to 999,999	$1,000,000 or more
Minority (N=400)	24.2%	34.3	15.7	18.5	4.0	3.2
Non-minority (N=2370)	16.2	28.9	18.1	27.2	4.9	4.7
Column Total	17.4	29.6	17.8	25.9	4.8	4.5

SOURCE: Task Force Questionnaire

CHART 2

Gross Receipts of Sole Proprietorships for Firms Owned by Women: 1972



SOURCE: U.S. Department of Commerce, *Women-Owned Businesses, 1972*, 1976, p. 241.

The pattern of business ownership by minority women does not differ significantly from that of ownership by all women.(80) We can conclude that if tax advantages were increased for sole proprietorships, it would not favor majority over minority women.

In 1972, almost half of all women-owned firms had gross receipts of less than $5,000 (201,623 firms out of a total of 402,025). As can be seen in Chart 3, the number earning more than $5,000 drops sharply. This is consistent with 1972 data that indicate that two-thirds of all small firms made under $25,000 in gross receipts that year. Data from the Task Force Questionnaire shows a very different picture. (See Chart 4.) Only 17.4 percent of the respondents had gross receipts in 1977 of $10,000 or less in contrast with 66.8 percent in 1972.

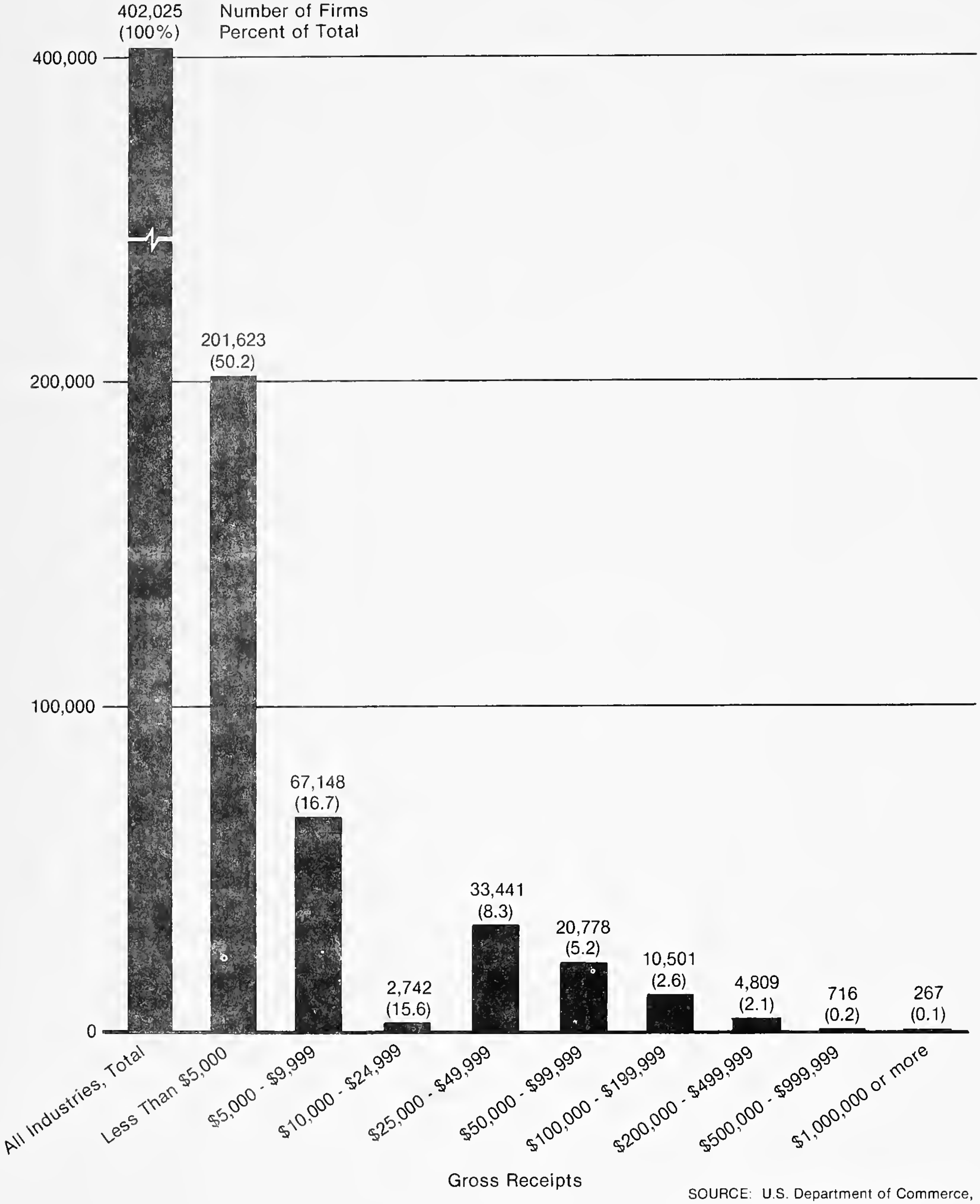
Minority women-owned firms also fit this pattern, with few bringing in sizeable receipts. Again, approximately half of all minority-women-owned firms earned less than $5,000 (15,601 out of a total of 33,810). This similarity of pattern indicates majority and minority women business owners are similarly affected by the tax code.(81)

Sole proprietorships are not taxed as business entities. Income from a sole proprietorship is taxed as a part of the total gross income received by the individual owner. The sole proprietor is able to deduct all business expenses, and the sole proprietorship is part of the graduated and progressive individual tax system, with rates ranging from zero to 70 percent. Thus, sole proprietors can benefit from the advantages accorded to the lowest income taxpayers.(82) Sole proprietors would be interested in tax reductions for individuals, for these reductions would increase their after-tax income and ability to place more capital into their businesses.

In addition to deductions from taxable income, the sole proprietor, as he or she files Form 1040 as an individual taxpayer, has certain tax credits. These are deductions from the tax liability, or income tax owed the Federal government, rather than deductions which reduce the income on which a sole proprietor and individual figure the tax owed. The three major tax credits that affect small business are the investment tax credit (Form 3468), the Work Incentive (WIN) Credit (Form 4874), and the New Jobs Credit (Form 5884). The WIN Credit enables an employer to deduct 20 percent of the first 12 months of an employee's salary who was hired under this program. The Jobs Tax Credit was intended to encourage employers to create new jobs and is paid under a formula that

CHART 3

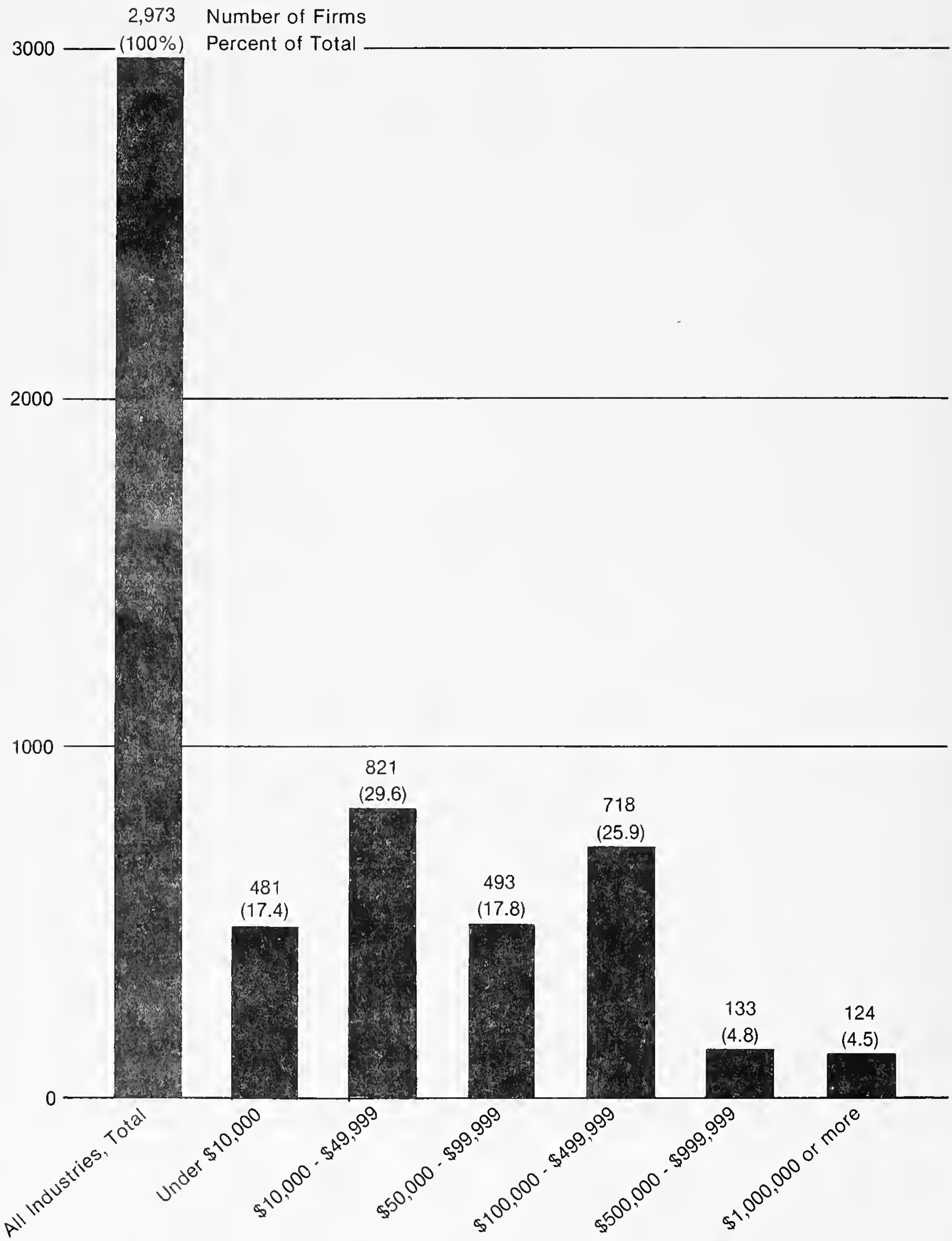
Gross Receipts of Sole Proprietorships for Firms Owned by Women: 1972



SOURCE: U.S. Department of Commerce, Women-Owned Businesses, 1972, 1976, p. 239.

CHART 4

Gross Receipts of Women-Owned Firms: 1977



SOURCE: Task Force Questionnaire.

is based on the amount of Federal Unemployment Tax. (It is 50 percent of the amount by which FUTA wages paid during 1978 exceed 102 percent of FUTA wages paid during 1977). The ten percent Investment Tax Credit is for new or used property acquired for use in the business during the tax year. Unlike the depreciation deduction, the investment tax credit applies only to tangible property such as machinery and not to buildings; further, the property must be depreciable and have a useful life of at least three years. The Administration has proposed that this credit be extended to industrial buildings, but in no case does it extend to working, office, sales or store space; warehouses; garages; railways or bus stations.(83) This means that certain kinds of women-owned business, namely those in manufacturing, receive larger tax credits than those in the service industry.

In summary, sole proprietorships deduct from their gross receipts almost every cost of doing business. Receipts minus costs equals the profits on which taxes are paid. Thus, as far as the tax code is concerned, there is little more that can be done to assist sole proprietorships. The tax credits discussed above apply to the two major components of business, capital and labor, but the great majority of women-owned small businesses use little of either. Only about 13 percent of all women-owned firms surveyed in 1972 hired any employees, and these hired very few.(84) As mentioned earlier, respondents to the Task Force questionnaire reported 29 percent of the women-owned businesses had no employees.

PARTNERSHIPS: A partnership is the unincorporated relationship existing between two or more persons who join together to carry on a trade or business with each person contributing money, property, labor, or skill and each expecting to share in the profits and losses of the business. For tax purposes, the term "partnership" may also include syndicates, groups, pools, joint ventures or other unincorporated groups not classified as trusts, estates or corporations. Important factors in determining whether or not the relationship is a partnership are the parties' conduct in carrying out the provisions of the agreement, the testimony of disinterested persons, the relationship of the parties, and the abilities and contributions of each. Thus, co-ownership is a joint undertaking merely to share expenses, not a partnership. A family partnership is one whose members are related through blood or marriage and a family member is recognized as a partner if he or she has a capital interest where capital is the material income-producing factor, or where the individual contributes substantial vital services where capital is not a material income-producing factor.(85)

In 1972 very few women-owned businesses were partnerships, only about 1.7 percent. The Task Force Questionnaire showed 23.7 percent of respondents had organized as partnerships.

Women-owned businesses in the form of partnerships accounted for seven percent of the gross receipts of all women-owned businesses -- $564 million out of a total of over $8 billion in 1972. Retail trade far outdistanced all other businesses in the amount of gross receipts. There is a slight difference in the rank ordering of types of businesses between majority and minority-women-owned firms, but receipts are so small that there are no implications for taxation.

Partnership profits and other gains are not taxed to the partnership. Instead, each partner determines his or her income as an individual taxpayer. However, choices determining computation of the partnership's income are determined by the partnership and not the individual partners. Such elections include the methods of accounting, computing depreciation, and amortizing organization fees.(86) Each partner is required to file a Form 1065; however, this form only serves to indicate to the Internal Revenue Service the amount and kind of income, deductions, and credit that the individual partners ought to report on their individual tax returns as their share of the income in the partnership. The distributive share is reported even if not actually distributed. Each partner's share is commingled with all other reportable income on his or her Form 1040. In the case of a loss, a deduction on the individual return to the extent of the adjusted basis of the partner's interest in the partnership is allowed.(87)

The main interest of partnerships is in tax relief for individual taxpayers. Thus partnerships would benefit from the Administration's proposals to reduce the share of the total income tax burden for each income class through $30,000.(88) This reduction would especially aid women-owned businesses, which often have incomes falling well within this range.

<u>CORPORATIONS</u>: A corporation is a business legally incorporated under state laws. It can take various forms, the most well-known and widely used is the joint stock company. For tax purposes, businesses operating in other forms may be treated as corporations if they have the characteristics of corporations. The tax treatment of corporations differs markedly from that of sole proprietorships and partnerships. Only corporations are taxed

separately as businesses. That is, the tax law treats corporations as entities separate and apart from their individual shareholder/owners. Corporate profits are taxed to the corporation and when the profits are distributed as dividends, the individual shareholders are also taxed. On the other hand, losses sustained by a corporation are not available as deductions to the stockholders.(89)

The Internal Revenue Code enables some corporations to elect the status of "Subchapter S corporations," under which they are not to be taxed as corporations, thus avoiding the double tax, but in a manner similar to partnerships. That is, the Subchapter S corporation, itself, does not pay taxes (except that it may be subject to capital gains taxes if its gains exceed $25,000). Rather, the individual shareholders include in their individual gross incomes distributive portions of the corporation's profit or loss.(90)

Subchapter S corporations are generally limited and are best suited for small business. However, any group of shareholders may elect to be a Subchapter S corporation so long as they meet <u>all</u> <u>six</u> of the following requirements:

1. The corporation may not have more than ten shareholders unless it has been in existence for five consecutive tax years. Then it may have up to 15 shareholders. The Administration has proposed that the number for all be raised to 15 to eliminate this technical and complicating exception.

2. The corporation may have only one class of stock.

3. The company must be a domestic corporation.

4. Only individuals, estates, and certain types of trusts may be shareholders (the Administration is attempting to simplify this rule) but no partnership or corporation may become a shareholder.

5. No non-resident alien can be a shareholder.

6. The corporation must not be a member of an affiliated group.(91)

The actual number of women-owned corporations is not known, because the 1972 Survey only counted Subchapter S corporations. In 1972 there were 1,251 women-owned

Subchapter S corporations, 0.3 percent of all women-owned firms. Minority women-owned corporations totaled 486. Once again, the patterns by industry for majority and minority women were almost identical with the largest numbers in retail trade and selective services. The Task Force Questionnaire showed 25.3 percent of respondents to be stockholders in corporations.

Despite their small number in 1972, women-owned Subchapter S corporations accounted for four percent of the receipts of all women-owned businesses ($356,665,000). Minority women-owned corporations earned $132,045,000 in gross receipts.(92)

The corporate income tax is structured so that a corporation pays tax at a rate of 20 percent on the first $25,000 of corporate income, 22 percent on the next $25,000 and 48 percent (the 22 pecent plus a surtax of 26 percent) on all income over $50,000.(93) Exemption from the 26 percent surtax is in itself a substantial tax benefit to the corporation whose income does not exceed $50,000. The Carter proposals would have an effect on small corporations by reducing the tax rate to 18 percent on the first $25,000 of income; 20 percent on the second $25,000; and, when fully phased in, to 44 percent on all income over $50,000.(94) The tax savings on the proposal would be of proportionately greater significance to smaller corporations, but in absolute dollars the savings would be much larger for major corporations. The President's stated aim is to deal with the inadequate capital spending in the U.S. during the past several years and to help to insure increased capital formation.(95)

General corporations file a Form 1120. In computing taxable income they take the same deductions that apply to individuals and, in addition, are eligible for special corporate deductions.(96) Since few women-owned corporations appear to be in the class of general corporations, subsequent discussion will concentrate on Subchapter S corporations.

Subchapter S corporations file a Form 1120S. In general, each shareholder must report as gross income his or her pro rata share of the corporation's taxable income. Under certain conditions, a Subchapter S corporation must pay a capital gains tax. However, very few women-owned Subchapter S corporations are subject to this capital gains tax. Subchapter S corporations are not eligible for the special deductions of general corporations.(97)

To summarize, major tax reform and reduction will not assist women business owners significantly. To understand why this is so, it is important to place these businesses and all small businesses in perspective in the economy. Since taxes are paid on profits, we want to call attention to the low income of small businesses in general, women-owned businesses among them. In fact women-owned small businesses have even lower income than small businesses in general.

In 1971, about 32 percent of all small businesses filing with the IRS showed no income or a deficit. Of the 8.5 million profitable firms (including farms) 75 percent had average taxable incomes of less than $10,000 and paid a Federal income tax of under $1,000.(98)

Since most small businesses have extremely low earnings bases from which to generate additional capital, even large reductions in the tax rate at the lowest levels of small business income will provide little help in significantly increasing earnings either for cash-flow or for minimal investment. However, reform and simplification of income tax forms required can lower the cost of tax compliance.

Tax Provisions Governing Small Business

Each year many proposals are made to change the tax code to assist small business. Those relating to establishing a small business, to businesses having gross receipts of under $50,000, and to individuals or firms providing venture capital will be reviewed in this section.

AMORTIZATION: Of particular importance to small business is the deduction of start-up expenses. Generally, the tax code does not permit these expenses to be deducted immediately, but, rather, allows them to be amortized (that is, deducted in equal amounts over a set time period, generally not less than five years). The following start-up expenses can be amortized: cost of acquiring a lease, research and experimental expenses, interest and real property taxes on construction used for business, legal and accounting fees for initial organization; bond premiums; temporary costs of directors; costs of organizational meetings; and on-the-job training and child care facilities. A table of amortization is supplied by the IRS to simplify the procedure.(99)

Small businesspeople feel that the amortization of start-up expenses should be possible automatically without the taxpayer having to formally file the election on his or her tax return. SBA's Office of Advocacy recommended in June 1977 that the limitations on the types of expenditures be broadened to include the costs of obtaining initial capitalization, syndication expenses, and trademarks and trade names, precisely those expenses now excluded. The purchase of good will is also recommended for inclusion.(100) Current Administration proposals do not include any further liberalization of the amortization rules.

PAYMENT OF TAX IN EARLY YEARS OF OPERATION: The tax code does not raise a barrier to fledgling businesses. Although businesses must file income tax returns, this does not mean that they pay tax. Taxes are paid on profits and if there is no profit, which is usual in the first years of operations, then no tax is paid. Absence of income does not prevent a businessperson from saving the ordinary and necessary expenses directly connected with his or her trade, business, or profession for deducting in later tax years.

PAYROLL TAXES: A major complaint of small business is the administrative burden of paying payroll taxes. In 1977 the Commission on Federal Paperwork reiterated at Congressional oversight hearings that payroll tax returns are the most costly reports for most small businesses to prepare. For these, as well as for other requirements, the Internal Revenue Code and its related regulations have become more and more complex, resulting in increasingly burdensome reporting requirements. Because the small business does not have ready access to resources such as lawyers and CPAs, complying with tax laws has a prohibitively high cost. In the case of payroll taxes, the relative cost of compliance with the regulations is far greater for a small business than a large corporation, thus making the burden of compliance highly regressive. Small businesspeople want and need a simpler tax structure.(101)

The Treasury Department is sympathetic to the needs of small businesspersons to be relieved of some of the paperwork burden and complexity of tax compliance. On the other hand, the integrity of the withholding tax system, which collects a major portion of all taxes, must be protected. SBA's Office of Advocacy recommended in June 1977 that any employee making less than $200 a calender quarter not be classified as an employee for payroll and withholding tax purposes. But past IRS surveys indicate that such a rule would lead to substantial amounts of income going unreported by taxpayers.

Another complaint dealing with payroll taxes is a financial one. Business taxpayers pay their taxes on an estimated basis in quarterly installments. This system was developed in the late 1950's in an attempt to equalize tax burden between businesses and individuals. Although all taxes were due on April 15, employees had their taxes removed each pay period, while employers had the use of their full income without tax deductions all year long. However, with the current quarterly payments, if a small business profit is not maintained, the excess of estimated tax is not refunded until the following annual income tax return is filed. Since financial reverses from profit to loss may cause a hardship on small business, SBA's Office of Advocacy recommended that a taxpayer get a quick refund of estimated tax when it became clear that the amounts paid will be clearly in excess of the tax liability.(102) The Treasury Small Business Advisory Committee and the IRS should prepare a simpler estimated tax form and study the timing of payment of refunds of overpaid taxes.

RETIREMENT--EMPLOYEE RETIREMENT INCOME SECURITY ACT (ERISA): Sponsored by IRS's Small Business Advisory Committee in 1974, the Act has, in actual practice, placed great burdens on small business. It should be simplified to permit participation by small businesses which cannot afford to administer retirement plans under the new laws and regulations. Congress should consider simplifying the law for plans covering 100 employees or less, thus reducing reporting costs and administrative burdens.(103) A standard plan for every type of business with 10 employees or less should be developed. This would reduce costs to small businesses but its impact on women-owned business would be limited to those that have employees.

RETIREMENT SECURITY OF THE SMALL BUSINESS OWNER: A recurring complaint is that existing retirement plans are not responsive to the need of small businesses because they are complicated and expensive to establish, place unwarranted emphasis on the legal form of business organization and make compliance too complex.(104) This issue should be investigated and the tax code amended to simplify retirement plan requirements for both owners and employees.

Taxes Related to Business Operations

Capital is the most important need of small business. The inaccessibility of traditional outside financing sources forces small businesses to finance themselves largely by reinvestment of earnings, which must be sufficient for both current operations and future expansion. Profits left after taxes are of vital importance to small business. Besides internal cash flow a small business' major source of working capital is borrowing, and ability to obtain credit depends, in part, upon profits. Proposals to reduce taxes on small business are directed at the difficulty of forming capital.(105)

ADDITIONAL GRADUATION OF THE CORPORATE TAX: The tax code first instituted a graduated rate for corporate taxes in 1936. Two years later the code made a sharp distinction between corporations making up to $25,000 per year and those earning more. In 1940 a system of graduated steps was established, and ten years later, in 1950, the current concept of normal tax and corporate surtax was introduced, with the surtax being levied against the amount earned over $25,000. By 1961 the effective tax rate on corporations for all income over $25,000 was 48 percent. It was not until 1975 that the first major reduction in corporate taxes was made. This tax change reduced the corporate tax rate on the first $25,000 of earnings from 22 to 20 percent. The tax rate on earnings between $25,000 and $50,000 was lowered from 48 to 22 percent. A surtax of 26 percent was added on income over $50,000, hence making the effective rate of tax on all income over $50,000 equal to the former 48 percent. It is this structure which the Carter Administration now proposes to reduce slightly, the tax on the first $25,000 would drop to 18 percent; that on the second $25,000 would fall to 20 percent; and that on all income over $50,000 would drop first to 45 percent, then permanently to 44 percent.(106)

It is believed that small business will not be particularly pleased with this proposal even though it would result in tax reduction for most. Instead, each year a more progressive rate structure is suggested, for example, in December 1976 the Treasury Small Business Advisory Committee on Economic Policy called for a four-step graduation (0 to $9,999; $10,000 to $49,999; $50,000 to $199,999; and $200,000 and over). In the spring of 1977 a former IRS Commissioner, Randolph Thrower, then a member of the Advisory Committee, told the House Ways and Means Committee that inflation-adjustable graduated rates for small incorporated businesses are probably the best form of relief. The Advisory Committee also recommended an alternative, such as increasing the surtax exemption or maintaining the current form but spreading out the rates to 10 percent, 28 percent and 45 percent.(107)

DEPRECIATION AND SIMPLIFICATION OF ASSET DEPRECIATION RANGE (ADR): All businesses are able to recover the cost of certain types of tangible and intangible business property through the process of depreciation. Each year the taxpayer deducts as depreciation a reasonable allowance for the exhaustion, wear and tear, and obsolescence of depreciable property utilized in the production of income. Property so depreciated must have a limited useful life. The shorter the useful life of equipment, the greater is the amount allowed for depreciation. Depreciation is a major deduction from income for small business.

The tax code permits property with a useful life of more than one year to be depreciated. Examples of property which may be depreciated are buildings, machinery, trucks and equipment including retail trade and office equipment, patents and copyrights, franchises and other intangibles as designs. Items with indefinite lives, and therefore not subject to depreciation, are good will, trademarks and trade names, and land. In addition, a taxpayer may deduct 20 percent of the cost of new or used tangible property having a useful life of six years and up to a cost of $10,000 ($20,000 if a joint return) in the first year in which such property is depreciated. Depreciation begins to be taken in the year in which the property is acquired.(108)

The small businesswoman or man has had problems in computing depreciation. Businesses now have the choice of claiming depreciation on the basis of "facts and circumstances" applicable to their situation, or using an asset depreciation range and class life system developed by the Internal Revenue Service, based on standard depreciation lives. Substantial tax benefits are derived through use of the published depreciation lives and the additional range, which allows a business to select a depreciable life from 20 percent below to 20 percent above the established class lives. For example, if the useful life is ten years the property can be depreciated on the basis of a useful life of from eight to twelve years. Generally, the ADR system permits more rapid writeoffs of costs of productive assets than would be the case under conventional rules.(109) Taxpayers who do not use the ADR lives are also subject to challenge by IRS auditors.

Although the standandized treatment was designed to prevent disputes between the taxpayer and IRS, it has ended up imposing such burdensome and complicated reporting requirements on small businesspeople that, as a practical matter, this system is not available to small business. In effect, IRS regulations have become highly discriminatory in that the most advantageous depreciation method cannot readily be used by small business.(110)

Recognizing that such complexities in tax laws are especially burdensome to the small businessperson, the Carter

Administration has proposed the adoption of a simplified table by which the small businessperson may determine the useful life of property without complex recordkeeping requirements The simplified tables maintain the 20 percent range feature, and would enable the taxpayer to ignore salvage value. He or she would not be required to participate in surveys. It is expected that the special depreciation system would be available to more than 90 percent of all small businesses regardless of organizational form.(111)

This proposal would not only ease the recordkeeping burdens of small businesswomen but would be of great assistance in increasing retained earnings of every businesswoman regardless of the form of organization chosen. Its impact would vary depending upon the industry her business is in. For example, women in transportation and manufacturing would benefit more than those in the retail or service trades.

<u>DEPRECIATION AMOUNTS AND TIMEPERIODS</u>: While the President has recognized, and proposed remedies to, the problems of computing depreciation using ADR, there are no current recommendations for further shortening the time period or permitting a lump-sum deduction. In the past a number of suggestions have been made. In December 1976 the Treasury Small Business Advisory Committee on Economic Policy recommended that a taxpayer be permitted to write off any amount up to and including 100 percent of asset value in the year of acquisition with a limit of $200,000 per year. This was also one of the principal recommendations of the Small Business Administration Venture and Equity Capital Task Force chaired by William Casey. In May 1977 the Smaller Business Association of New England advanced a similar proposal. They asked Congress to allow a deduction for the full cost of the first $200,000 of depreciable personal and real property, the timing of the deduction to be totally within the control of the taxpayer. The suggestion would eliminate the need for preparation of detailed depreciation records on each property item.

In 1977 the Council of Small and Independent Business Organizations and a group of five regional small business organizations recommended to Congress that they consider an accelerated capital recovery program under which there would be: (1) a two-year depreciation period for vehicles, equipment, and tools up to a limit of $100,000 annually; (2) a five-year depreciation for machinery, transportation equipment, office furnishings and leasehold improvements, with a similar $100,000 annual limit; and (3) a ten-year depreciation for all forms of commercial structures up to a limit of $200,000 annually. This proposal was drafted into

Section 403, Adjustment of Depreciation Schedules, of the proposed "Small Business Venture Capital Act of 1977 (S.1815)," which was introduced in the Senate in June 1977. The Senate Select Small Business Committee offered a similar proposal in early 1978. The Committee tested these different alternatives for calculating depreciation and found that the most promising for small business was three-year life, with one-third of the investment credit retained with an average gain of about $410 per company. The Committee also proposed that their plan apply to business equipment purchases of all kinds rather than to the Administration's 18 categories only. The Committee held that many small business organizations would find their plan to be a major simplification which would stabilize the service life of the productive assets and would decrease uncertainty. In addition, the requirements for expensive professional accounting advice would be reduced.

In June of 1977 the SBA Office of Advocacy called for a new method of computing depreciation in order to circumvent inflation. The calculation of the deductible amount is now based upon the historical cost of the asset which would have to be replaced at a higher cost due to inflation. SBA recommended that small businesses be permitted to depreciate all depreciable assets at twice the straight-line rate, and, in view of this increase, that the additional first-year allowance be repealed. This proposal would provide funds quickly through a tax reduction and would also permit depreciation which would more realistically reflect the economic erosion of inflation.(112)

All of these proposals provide for more liberal depreciation than the Administration has itself proposed to Congress. Most of the proposals subsidize certain kinds of small business at the expense of others to the extent that some sorts of depreciable property have a longer real life than others, yet all have the same write-off or depreciable timetable. There is also a subsidy in favor of small business over larger business due to the dollar limitations in the suggestions. On the other hand, Administration proposals develop a set of simplified tables which take into account every kind of business and the average length of life for depreciable property, as measured by experience. Treasury's tables would reduce the accounting cost and make it easier for small business to take the table or ADR option. In addition, the new tables would be useful to new businesses by decreasing the cost of making out their tax forms and decreasing uncertainty.(113)

INVESTMENT TAX CREDIT: A relatively small percentage of small businesses benefit from the investment tax credit. It does not generally assist women business owners, many of whom are in industries that require low capitalization. Increasing the investment tax credit would not assist small firms mainly because they use much labor relative to capital as a factor of production.

The investment tax credit plays a minimal role in the financial and tax planning of small business for two reasons. First, small business investments in any one year are typically modest; second, tax credits are only useful for profitable firms and many small businesses, especially those in operation for less than five years, do not show a profit. In short, since most women-owned businesses do not pay high taxes, the investment tax credit, which is a deduction from the tax owed the Federal government, is not much use in significantly increasing after-tax profits.(114)

The investment tax credit was originally established in 1961 to give an incentive for investment in new productive machinery. The purpose was to make the credit effective by aiming it at those industries that make investments. Since very few women-owned businesses are in the areas of manufacturing, construction, transportation and public utilities (only about 29,000 out of 402,000 in the 1972 survey), the investment tax credit does not serve to reduce the taxes of the bulk of women-owned businesses.(115)

The Carter Administration has proposed the following changes in the investment tax credit.

1. The ten percent rather than seven percent investment credit would become permanent. This provision would assist those women-owned businesses able to utilize the credit.

2. Eligibility would be extended to the construction and rehabilitation of industrial or manufacturing structures or those used by utilities. This provision is almost meaningless to women business owners. What has a greater impact is the fact that commercial buildings and retail stores are not eligible for the credit. For the handful who are covered, the proposal will simplify and lower the cost of compliance by reducing disputes with the IRS over what structural property qualifies for the credit.

3. The tax liability ceiling would be changed to a flat 90 percent of the total tax. Though the proposal's effectiveness is meant for businesses with relatively high investment needs and low taxable income, it is slightly detrimental to small businesses which can no longer use the investment tax credit to completely eliminate their entire tax. Under the proposed rule, the 90 percent ceiling means that ten percent of the tax must be paid.(116)

In practice, this change will affect fewer than 30,000 women business owners out of 402,000. And this number will be greatly reduced because many of the women-owned businesses in the capital-intensive industries do not make a large enough income to have a profit to pay a tax on, or pay such a low tax that ten percent of that tax will have no bearing on the ability to significantly increase after-tax profits. The negative effect will be minimal despite the fact that there is a detrimental impact in exchanging no tax for some tax.

Commercial buildings or intangible depreciable property were not included as eligible for the investment tax credit as recommended by SBA because the Treasury Department feels they are already receiving generous treatment under depreciation rules. However, industrial structures and machinery can be depreciated. Treasury might consider making the investment tax credit less biased against certain kinds of assets acquired by small commercial businesses that do not use machinery or heavy equipment or work in industrial buildings. Such a credit could be structured to prevent its use as a tax shelter. This would mean a restructuring of the tax credit(117) and, since it is of such limited use to small business, it appears better to press for increased employment credits. Strangely, this is a tax advantage to which labor-intensive small business seems to have given little thought.

<u>NEW JOBS CREDIT</u>: Small businesses need incentives, such as an employment tax credit, that are directly linked to their operations and employment, rather than to credit and capital formation.(118)

An employment tax would have positive effects on both employment and aggregate spending by reducing real labor costs, thus encouraging businesses to maintain or increase employment. The credit would also result in an increase in aggregate spending if the reduced cost of labor leads to a reduction in prices. It was from such macroeconomic thinking that the Government recommended the current jobs tax credit. As one witness told Congress, the benefits of employment credits to small business will far exceed the benefits from an investment tax credit or its increase. And firms can adjust their use of labor to changes in the employment credit rate faster than they can adjust capital to changes in the investment tax credit.(119)

Currently, there are two employment tax credits to employers. Under the WIN program (Work Incentive Program Tax Credit) 20 percent of the salary or wages paid for the first 12 months of work to someone hired under this program is subtracted from the tax liability. There is a limit on the amount of credit allowed. The credit is permitted only if the employment lasts for 180 days without termination. But the program, which is at first glance very attractive for the very small businessman or woman, has been laden with such complex and almost incomprehensible rules and administrative requirements that most small businesses are afraid to even attempt taking the credit.(120)

The Jobs Tax Credit is an incentive to create new jobs. In general the tax credit is based on the Federal Unemployment Tax Act wages (FUTA) paid during a calendar year and employers who do not pay this tax are not eligible to take the credit As the law now reads, for tax years beginning with 1978, the credit for new jobs is 50 percent of the amount of FUTA wages paid during the year which exceed 102 percent of the FUTA wages paid in 1977. Married persons filing separate returns have a credit limit of $50,000, unless only one spouse has an interest in the business creating the new job, and then that persons' credit limit in any one taxable year is $100,000. The only exception to this limit is the additional ten percent credit permitted for hiring handicapped employees.

Once the employment job tax credit has been computed, and it is $100,000 or less, the credit may be applied against the taxpayer's tax but only after that tax liability, (i.e., the amount owed the government,) has been reduced by the following credits: foreign tax credit, which does not pertain to most small businesses; credit for the elderly; investment credit, which would apply to only a handful of women-owned small businesses; contributions to candidates for public office; the general tax credit; and child care expenses. There is nothing to prevent the credit from eliminating the total tax liability. In addition, if the credit exceeds the tax due, it may be used in the 10-year carry-over formula (three years carry back, beginning with the earliest year; and several years carry forward). If after this length of time the credit has not been used up it is lost.(121)

The form of business organization also impacts upon the way the new job tax credit is taken. For partnerships it reduces the deduction for wages and salaries otherwise allowable to the partnership. The amount of the credit earned is apportioned pro rata among the partners and is shown on Schedule K-1 of Form 1065.

Subchapter S corporations compute the dollar amount of the credit in the same manner as partnerships. The amount earned by the credit is then apportioned pro rata among the shareholders on the last day of the tax year and is shown on Schedule K-1 of Form 1120S. The amount of credit that each shareholder may claim on his or her individual return cannot exceed the amount of his or her individual tax liability. The amount of credit allowed a partner or a shareholder of a Subchapter S corporation is further limited to the proportionate part of the tax for the year allocable to the taxpayer's interest in the partnership or Subchapter S corporation from which the credit is derived.(122)

Changes in the new jobs tax credit are needed. This credit would be of great benefit to small business in general and women-owned businesses in particular. It would increase employment and might encourage many women-owned businesses that do not now employ any full-time or part-time help to begin to do so. With employment experience women might consider expanding operations, which they might not do if they had to operate the business alone. Secondly, the new jobs credit is neutral, it does not discriminate in favor of one type of business over another. Suggestions for changes are as follows:

1. Eliminate the WIN jobs credit program altogether.

2. Provide, instead, for one, permanent, new jobs employment credit.

3. Make the calculation of the credit clear and simple and reduce the large administrative burden and current costs of compliance.

<u>MISCELLANEOUS--THE ESTATE TAX</u>: The Federal estate tax contains no structural bias against women business owners as compared to other business owners. Indeed, the estate tax marital deduction enables a husband who predeceases his spouse to pass separately-owned property equal to the greater of $250,000 or one-half of his adjusted gross estate to his surviving spouse free of estate tax. (This applies equally to husbands inheriting from wives who predecease them; the

tax code makes no distinction. However, our discussion here focuses on the wife who inherits a business, since that is the topic of this report.) Thus, where the subject of the marital bequest is a business interest, surviving wives may be viewed by some as tax-favored when compared to non-spouse recipients of a decedent's property. There are, however, problems of applying the statutory structure which, as a practical matter, may have an impact upon surviving wives. These problems relate to the difficulty of determining, in a spousal business, what precisely is to be included in a deceased husband's estate.

The amount of the jointly-owned property included in the estate of the first owner to die is determined by reference to the proportion of the consideration for the acquisition of the property supplied by the decedent. Problems then arise because title to property may be held in the name of the decedent, but some other person may allege he or she was actually the owner of all or a portion of it. Or tracing contributions to determine the includible amount may often be difficult, particularly where the contribution has its source in services.

These problems exist whether or not the individuals involved are spouses. However, the issue may be exacerbated in the spousal case because of the reluctance generally of many state courts to hold, in the absence of a written agreement enforceable under local law, that services rendered by a wife constitute statutory "consideration" for the acquisition of the property.

To illustrate, assume a husband establishes a sole proprietorship or corporation. He supplies all the initial capital and takes title of all the business assets or stock. Thereafter, his wife contributes her time, labor, and, perhaps, some funds, but none of it is documented. On the basis of the documented facts, if the husband dies first the entire value of the business or stock is included in his gross estate. To reach any different result, the executor of the decedent's estate must prove either that a specific portion of the business or stock was actually owned by the wife, despite title being held by the husband, or that the business or stock was jointly owned, in which case the consideration supplied by the wife must be known to determine the amount includable in the husband's estate. If the executor prevails, the husband's estate is reduced, the estate tax is reduced, and the wife has additional capital to maintain or expand the business.

The answer to the problem is not to create special rules for spouses, but rather to require that spousal businesses be conducted on the same basis as businesses which involve unrelated parties.

The important point to make for the purposes of this report is to recommend that all practical means be used to bring this estate tax information to the attention of women who contribute funds, goods, or services to a business operated jointly with their husbands, and to urge them to properly document their interest against the possibility that their husbands predecease them. By thus reducing their estate tax, they will protect their business capital.(123)

Taxation to Encourage Venture Capital

One of the greatest problems for small business is finding sources of capital, for start-ups and continued operations, and for expansion, for without such funds it is difficult to obtain significant credit financing. Therefore, small business advocates join other business-people in recommending changes in the tax code that will provide for easier entry and withdrawal of venture capital and to facilitate the internal generation of capital.(124) Given this, small business is expected to react negatively to some of the Administration's current tax proposals claiming they do not provide enough incentives for venture capital.

The majority of small businesses have no direct need for traditional venture capital and, in fact, venture capital has never really flowed to small businesses. As mentioned earlier, venture capital firms prefer deals in the $125,000 and up range. It appears that small business has confused the situation that existed some time ago, when small business was the recipient of venture capital investment, with the situation today in which venture capital is going to smaller companies which are founded by managers with experience in large and sophisticated firms, and which very soon become medium-sized.(125) Therefore, tax aids to venture capitalists will provide little if any aid to today's small business. According to many people, there is an element of the chicken and the egg problem in the Administration's argument. When capital gains were taxed at an appreciably lower rate, and when capital losses could be more easily taken, and when stock market regulation and economic conditions facilitated stock issues from small businesses, there was venture capital available. It is unlikely that changing one of these adverse conditions would markedly increase venture capital funds, a more systematic approach would be necessary. The fact that such changes would make the rich richer is, perhaps, unfortunate from an equity standpoint, but it is the rich, and only the rich, who can afford to take the risks inherent in venture-type investments. If small business is, indeed, indispensible to the American way of life, mechanisms must be found to make such businesses viable. If rich people's money is not to be used, then the Federal government will have to fill the void by direct funding programs using general revenues.

In the interim, we feel that small business should be concerned about obtaining commercial bank credit, and financial and non-financial assistance, <u>i.e</u>. management and technical assistance from Federal programs. Venture capital, particularly that which it is hoped will be called out by current proposed changes in the tax code, will <u>not</u> meet these needs. Only direct programs which help to develop human resources can help now and such assistance can come from either the public or the private sector.

In summary, the Administration believes that proposed, changes in the capital gains and losses provisions of the tax code would not increase the supply of the kind of venture capital needed by most small businesses in the United States. Therefore, solution to the problem of capital formation for these small businesses must be found outside the tax code(126) in <u>direct</u> aid that looks to the development of human as well as economic capital. The Study Team feels more effort is needed to investigate alternatives and develop new approaches to supplying funds for venture capital investment.

<u>LOSSES ON SMALL BUSINESS STOCK</u>: Special tax treatment of losses on small business stock is designed to encourage investment in small businesses by decreasing the risk of such investment. Section 1244 of the tax code specifies that such stock must be common stock of a domestic corporation, issued under a specific plan adopted by the company in return for money or property but not for securities. Only the original individual owner is permitted to deduct an ordinary loss rather than a capital loss.(127) Ability to take the stock loss as ordinary loss provides much more favorable tax treatment than loss on the sale of other capital assets.

There are size limitations on eligibility written into Section 1244. The problem is that inflation has eroded the dollar's value and effectively tightened these limits. The Carter Administration realized that these limitations would have to be changed in order to make it easier to attract outside equity capital to small business and to decrease the risk associated with failure.(128) Reforms have been proposed.

The corporation issuing stock eligible for Section 1244 benefits must be below a certain size, the total stock offering plus the equity capital of the corporation may not exceed $1,000,000. The President is proposing that the $1,000,000 limit on the corporation's equity capital be completely eliminated, thus relaxing the size limits.

A corporation may only issue up to $500,000 worth of Section 1244 stock. The Administration proposals would double this issue limit to $1,000,000.

Other technical requirements that needlessly restrict the ability of the small business corporation to issue Section 1244 stock would be eliminated. This is particularly important because the requirements for getting tax benefits from Section 1244 are unduly complex and failure to comply strictly with these requirements results in denial of ordinary loss treatment.

If the President's tax proposal is passed by Congress the amount of ordinary loss that an individual may declare on his or her income tax return would be doubled from $25,000 per person or $50,000 in the case of a joint return to $50,000 and $100,000. (Gains on Section 1244 stocks are treated as capital gains.) If Congress passes this proposal it will be put into effect in the 1979 tax year. The proposal has no significant revenue effect.(129) Although similar or identical versions of this proposal have circulated for several years, they have not until now received strong Administration support.(130)

Women-owned corporations would benefit <u>significantly</u> from this tax change. The Study Team strongly supports passage of this tax proposal and recommends review of this provision and the impact of inflation upon it, so that periodic changes in the limits permitted for loan loss can be made if warranted. Section 1244 is one of the best incentives for investment in small businesses and its benefits and advantages should not be weakened.

<u>SMALL BUSINESS INVESTMENT CORPORATIONS</u>: Small Business Investment Corporations, SBICs, are private corporations licensed by the Federal Government in an effort to provide more venture capital to small business. Liberal tax concessions have been provided for both SBICs and their investors in sections 1242 and 1243 of the tax code. SBICs generally make their investments by purchasing a convertible debenture, that is, a bond which may at some point and under certain

conditions be converted into common stock. This is the method by which most SBICs make their investment secure, because if the business is successful the SBIC can convert the debenture to stock and receive tax-free dividends. If it is unsuccessful the debenture secures the SBIC's rights as a creditor. The SBIC has a benefit both ways.(131)

SBICs are permitted to deduct from their income tax any dividends received from the small domestic businesses in which they have invested. The exemption of these dividends from taxation is a high incentive to investment. In addition, the surtax on accumulated earnings that might be considered excessive by the IRS in other circumstances is not applicable to SBICs. Further, liberal bad debt reserve privileges may permit a postponement of income taxes. And finally, SBICs are not subject to the personal holding company tax.(132)

The provisions in the tax code governing the gains and losses of SBICs and SBIC shareholders, as differentiated from shareholders in the small businesses themselves, are also liberal and are structured so as to attract venture capital to small business. Any gain on the disposition, by sale or other means, of small business company stock is taxed as capital gain, that is 50 percent of the gain is taxable, rather than the full amount. The alternative capital gains computation for corporations is also available -- 30 percent of the net long-term (an asset held 12 months or more) capital gain over the net short-term capital loss. The amount arrived at by whichever method is more favorable is then added to shareholder individual income and taxed accordingly.

SBICs and shareholders also are entitled to liberal tax provisions governing operating losses as well as losses when the small business stock is sold. Net operating losses may be carried back ten years. Losses on the sale or disposition of convertible debentures, stock or loans is taxed at the more favorable ordinary loss rates, rather than at capital loss rates. All of the amount of the loss is deductible against ordinary income and there is no limit on how much may be deducted. The SBIC stockholder may likewise deduct from his or her income any losses suffered from the disposition of SBIC stock.(133)

Despite these favorable tax provisions, SBA's Office of Advocacy in June 1977 made a number of recommendations about further liberalizing the taxation of SBICs. SBA recommends that the tax code be amended to allow a deduction for additions to loss reserves of SBICs for the equity portion of their portfolios as an alternative to waiting until the investment actually is sold or becomes worthless. This provision is already permitted for additions to reserves for losses from debt instruments. The Treasury Department is of the opinion that because of the special tax breaks SBICs already have and the fact that their dividends from stock are tax-free this provision is not needed. SBICs have stock, on some of which they take a loss and on others of which they make a gain, but in the long run they must expect to profit. Thus further tax incentives of this kind will not call out more investment.(134)

The Treasury Department feels that the liberal tax treatment of dividends to SBICs and other corporations which receive dividends from corporations, as opposed to an individual receiving a dividend from a corporation, eliminates, for now, the need for this suggestion. Under the current tax code, dividends are taxed twice, once to the corporation which made the profits and again to the individual who received the dividend as income; so, the Government taxes dividends to intermediary corporations very lightly, at a rate not exceeding 7.2 percent. If SBICs make money from their investments and they receive lightly-taxed dividends, there is no need for additional tax incentives to investment. Most of the SBIC venture capital firms are owned by large corporations or rich individuals and these corporations and individuals already have enough incentives to invest under the current tax code.(135)

<u>CAPITAL GAINS</u>: Many people believe that the capital gains tax has become so high that it no longer serves as an incentive to long-term capital investment. The movement of the capital gains rates toward the level of tax rates on earned income has altered the risk-reward relationship for investors. This is likely to have the greatest impact on equity investment in small businesses where capital is already scarce and the risk of loss is greatest.(136) If the Administration's proposal is accepted by Congress, <u>all capital gains</u> will be taxed alike: 50 percent of half of the gain will be included in gross income on which the taxpayer's tax is based. This income is then taxed at rates which currently go as high as 70 percent but are proposed to be reduced to 68 percent. The alternative tax provision will be eliminated. That is, taxpayers whose capital gains exceed $50,000 may no longer tax the first $50,000 at the rate of 25 percent. Those taxpayers making occasional large capital gains, over $50,000 in one year, may use income averaging to achieve tax relief.(137)

But there are those who feel that this simplification of the tax code may have an effect on the supply of venture capital to small business,(138) and alternative suggestions have been proposed to encourage investment in small business by using a 25 percent tax rate on capital gains in a strictly limited way.

The Treasury Department has not reacted positively to these and similar recommendations regarding favorable tax treatment for capital gains. The Department is of the opinion that such tax advantages to the investor would aid only the wealthy rather than benefiting the small business-person and little additional venture capital would be invested. Also, Treasury believes that the additional amount of capital forthcoming would be at a tremendous cost in tax revenues. Thus, it would be far cheaper for the Government to give direct grants or provide special loan programs (e.g., establish special investment companies like SBICs). Treasury feels the tax code is not the place to provide incentives for venture capital to small business. Women-owned businesses, like all small businesses, would be better assisted by direct loan programs rather than through changes in the tax code.(139)

What small businesses need is credit, tax changes will not encourage banks to lend if they do not think the venture is profitable. And, at the moment, most small businesses do not have problems getting credit for viable, profitable needs.

The main area to be addressed, then, is start-up capital and some form of investment credit for that factor of production which, in small business, is intensive -- labor. A new jobs tax credit has been suggested to assist small business.

But what small businesses really need is simplification of the paperwork involved in tax compliance. They need simpler tax forms and procedures. In 1964 it was noted that the small business was becoming a free tax-collecting agent for the Government with the costs of this collection being paid directly by the firm. Recordkeeping and reporting were considered complicated and burdensome 15 years ago and matters have only become worse. Many firms find it necessary to turn their tax compliance work over to a bookkeeper or accountant, many of whom are not sufficiently skilled in application of the tax code and who only serve to increase the cost of compliance. Many small businessmen and women lack a general knowledge of their tax responsibilities, according to the study done 15 years ago; and to a great extent this was due to an unwillingness or reluctance to make the effort to become better informed about tax matters. There was seldom any evidence of organized planning to meet the tax problem in a better fashion; in seeking tax help the cheapest help was equated with the best help.

What most small businesses need to know is how to find competent help. The two major tax problems of small business are lack of knowledgeable personnel and inadequate accounting. The businessman or woman also needs to pay better attention to the planning phase of taxes, particularly to State and local taxes, which, because they are deductible from the Federal tax, are not deemed to constitute a full burden.

The solutions to the high costs of compliance are not simple. Many of the solutions to these problems are not found in the tax code itself, nor even in the regulations, but in training. Again, the answer is direct assistance. The Treasury Department has proposed that the IRS, in conjunction with the Small Business Administration and the Commission on Government Paperwork, prepare a series of proposals that will:

1. reduce the number of forms that are required, especially the different types of forms;

2. simplify those forms that are necessary;

3. provide free tax compliance seminars;

4. set up a program whereby retired small businessmen/women and accountants can assist the small business owner; and

5. clarify the regulations under which the tax laws are implemented.

Most small businesses fill out income tax forms that are not complicated. What is complicated is understanding the regulations which govern deductions and credits and the ways by which it is required they be computed.(140) This type of assistance can be made available to small business now; major changes in the tax code would require a great deal of time and political activity.

CONCLUDING REMARKS: We started this paper with a description of sociological conditions which have produced a disparity in the distribution of economic rewards between men and women. The policy usefulness of much of the material contained in our report may be less than optimal -- primarily due to the almost total absence of hard data on women business owners. Many of our recommendations are aimed at treating the symptoms of the problem, not the problem, itself. More direct aid is essential for women entrepreneurs until they can compete on an equal footing with men. This will not, however, do much to change the underlying societal belief that women do not make good business people. The Federal government can do a great deal to change this image through its programs, but it will require that more affirmative steps be taken than has been the case in the past. B. F. Skinner believes that as one changes one's behavior, a change in attitude will occur to match the new behavior. It is certainly worth a try.

N O T E S

1. In order to elicit information from women entrepreneurs, the Task Force undertook a special inquiry so that women business owners today could provide a picture of how they see themselves. Due to the short time frame of the the Task Force, public hearings were not possible, therefore, an inquiry form was distributed through the regional offices of the Department of Commerce and the Small Business Administration, and women business and professional associations to elicit volunteer responses. In addition, public service announcements on national and local radio stations were used to obtain this volunteer input. This approach represented the most effective way of getting the greatest number of responses in the shortest time.

It should be noted that the information from these volunteer resources does not approximate scientific sampling. Therefore, this information cannot be compared to the existing data from the Bureau of the Census or the Bureau of Labor Statistics, nor can it be generalized to the population of all women entrepreneurs because of its public inquiry format. However, it has proven very useful in illuminating some of the barriers women entrepreneurs believe they face.

2. U.S. Department of Commerce, Situation Report (Washington, D.C., November 1977), p. 1; U.S. Small Business Administration, Office of Advocacy, The Study of Small Business, (Washington, D.C., June 1977), p. v; U.S. Congress,

House of Representatives, Women in Business, A Report of the Subcommittee on Minority Enterprise and General Oversight of the Committee on Small Business, No. 95-604, 95th Congress, 1st Session, 1977, pp. 2, 4.

3. Women in Business, Subcommittee Report, p. 7; U.S. Congress, House of Representatives, Women in Business, Hearings before the Committee on Small Business, Subcommittee on Minority Enterprise and General Oversight, April, May, June 1977, pp. 47, 101; Simone de Beauvior, The Second Sex, translated by J.M. Parshley (New York: Vintage Books, 1974), passim, see especially pp. 663-664, 666-668, 694, 780; Phyllis Chesler and Emily Jane Goodman, Women, Money and Power (New York: Bantam Books, 1976), pp. 11, 223, 252; Monthly Labor Review 97 (May 1974): 40; Eleanor Brantley Schwartz, "Entrepreneurship: A New Female Frontier," Journal of Business V (Winter 1976): pp. 62, 66, 67, 69; "A Close-up of Women in the U.S.," U.S. News and World Report, December 8, 1975, p. 73.

4. House of Representatives, Women in Business, Hearings, 1977, pp. 47, 101; Subcommittee Report 95-604, pp. 7, 14, 23; Helen S. Astin, Nancy Suniewick, and Susan Dweck, Women: A Bibliography on Their Education and Careers (New York: Behavioral Publications, 1974), pp. 1, 137, 139.

5. U.S. News and World Report, December 8, 1975, p. 57; Astin, et. al.; p. 45.

6. Margaret Hennig and Anne Jardim, The Managerial Woman (Garden City, New York: Anchor Press 1977), p. 109; Letter from Margaret Ann Watson to Patricia M. Harvey, March 3, 1978, pp. 3-4; See also Astin, et. al. pp. 62, 190, 202.

7. Astin, et. al., p. 128; Wyndam Robertson, "The Ten Highest-Ranking Women in Big Business," Fortune, April 1973, p. 87; "Still More Room at the Top," Newsweek, April 29, 1974, pp. 74, 79; Schwartz, p. 71.

8. Francine Blau Weisskoff, "Women's Place in the Labor Market," The American Economic Review, Papers and Proceedings LXII (May 1972): 161; Elizabeth Waldman and Beverly J. McEaddy, "Where Women Work - An Analysis by Industry and Occupation," The Monthly Labor Review 97 (May 1974): 3, 9; Beatrice G. Reubens and Edwin P. Reubens, "Women Workers, Nontraditional Occupations, and Full Employment," Paper presented in U.S. Congress, Joint Economic Committee, Subcommittee on Economic Stabilization, American Women

Workers in a Full Employment Economy, A Compendium of Papers, 95th Congress, 1st Session, 1977, p. 106; Council of Economic Advisors, Economic Report of the President 1973, p. 90.

9. It is interesting to note that the concentration of women-owned businesses into a few industries closely parallels the traditional or female occupations into which most women are clustered. For example, more women-owned businesses are in services than in any other industry and the service industry continues to rank first as the most important employer of women. The linkage between employment and business enterprise is seen on the low side as well; there are few women-owned businesses in those industries in which few women are employed.

10. Reubens and Reubens, Joint Economic Committee, 1977, p. 106.

11. U.S. News and World Report, December 8, 1975, p. 61; Barbara B. Reagan, "De Facto Job Segregation," Joint Economic Committee, 1977, p. 96; "Women Seek Equal Chances in Business," Commerce Today II (July 10, 1972): 5-6; Astin, et. al., pp. 133, 210; Schwartz, p. 62.

12. Reagan, Joint Economic Committee, 1977, p. 93; Reubens and Reubens, Joint Economic Committee, 1977, pp. 117, 124-125; Mary Hamblin and Michael J. Prell, "The Incomes of Men and Women: Why Do They Differ?" Federal Reserve Bank of Kansas City, Monthly Review (April 1973): 9-11; Women's Bureau, U.S. Department of Labor, The Earnings Between Women and Men, 1976, pp. 1, 6.

13. Ibid, pp. 1, 6.

14. Victor R. Fuchs, "Recent Trends and Long-Run Prospects for Female Earnings," The American Economic Review, Papers and Proceedings LXIV (May 1974): 236-242; Victor R. Fuchs, "Women's Earnings: Recent Trends and Long-Run Prospects," Monthly Labor Review 97 (May 1974): 23-26; Council of Economic Advisors, Economic Report of the President, 1973, p. 106.

15. Fuchs, The American Economic Review, pp. 236-242; Reubens and Reubens, Joint Economic Committee, 1977, pp. 121, 124.

16. U.S. News and World Report, December 8, 1975, p. 70.

17. Ibid,; Bureau of the Census, Statistical Abstracts of the United States, 1977, p. 540.

18. U.S. News and World Report, December 8, 1975, p. 70; Chesler and Goodman, p. 52, 57 note, 58; "Lady Capitalists," Wall Street Journal, 10 January 1966, p. 1.

19. Chesler and Goodman, p. 51; Paul Nelson, The Joy of Money (New York: Bantam Books, 1977), p. 3.

20. Chesler and Goodman, pp. 51, 53; Nelson, p. 3.

21. U.S. News and World Report, December 8, 1975, p. 70; Chesler and Goodman, p. 49; Wall Street Journal, 10 January 1966, p. 1.

22. U.S. News and World Report, December 8, 1975, p. 70.

23. Robertson, Fortune, April 1973, p. 86; Elisabeth Anthony Dexter, Colonial Women of Affairs: Women in Business and the Professions in America before 1776, Clifton, New Jersey, Augustus M. Kelley, reprint in 1972 of 1931 edition; and Career Women of America 1776-1840, Clifton, New Jersey, Augustus Kelley reprint in 1972 of 1950 edition.

24. James W. Schreier, The Female Entrepreneur: A Pilot Study (Milwaukee: The Center for Venture Management, March 1975), a survey of fourteen women business-owners in Milwaukee, Wisconsin; Schwartz, pp. 47-76.

25. Schwartz, pp. 47-59, 65-68, 71; Schreier, pp. 3-4, 6, 10-11, 13-14; Mary R. Sumner, "Women in the Business and Office Occupations as Depicted in the American Novel: 1890-1950" (Ph.D. Dissertation Rutgers University, the State University of New Jersey, 1977), abstracted in Dissertation Abstracts, January 1978, p. 3890-A; "Up the Ladder," Business Week Executive Portfolio, 1976, pp. 152, 159.

26. Schreier, pp. 8-9, 12; Joan Libman, "Going It Alone: Female Entrepreneurs Like Del Goetz Make 'Man's Work' Pay Off," Wall Street Journal, 22 August 1975, p. 19; Hennig and Jardim, pp. 27, 29; Schwartz, p. 68.

27. Hennig and Jardim, pp. 74, 112-113; Schwartz, pp. 66, 68; Schreier, p. 11.

28. Federal Home Loan Bank Board, "Report to the Task Force on Women Business Owners" (Washington, D.C., 1978), pp. 3-6.

29. "Competing with the Giants," Dun's Review 11 (October 1977): 46-52.

30. The description of the business should include:

1. The type of business: Is the business primarily merchandising, manufacturing, or service?

2. The status of the business: Is it a start-up? An expansion of a going concern? A take-over of an existing business?

3. The legal organization of the firms: Sole proprietorship, partnership, corporation or Sub-chapter S corporation?

4. Why is the business going to be profitable?

5. When will (did) the business open?

6. What hours of the day and days of the week will it be open?

7. If it is a seasonal business, or if the hours will adjust seasonally, the seasonality should be reflected in replies to 5 and 6.

For the new business the entrepreneur must go through a critical self examination. For instance:

1. Why will she be successful in this business?

2. What is her experience in this business?

3. Has she spoken with other people in this kind of business? What was their response?

4. Has she spoken with prospective lead suppliers to find out what managerial and/or technical help they will provide?

5. Has she asked about trade credit?

6. If she will be doing contract work, what are the terms? Reference any firm contract or letters of interest, and include it as a supporting document.

7. How will she offset slow payment by customers?

31. Insurance professionals can assist business owners in developing a four-stage strategy of "risk management" as follows: (1) All known risks are identified, these are the various property and liability losses which might be incurred; (2) the likelihood of occurrence and potential size of each possible loss is estimated; (3) ways to reduce the risk or control severity of the potential loss are developed; and (4) the best way to protect against the loss using insurance as the mechanism is defined. Warren C. Leoy, "Insurance for the Small Business," Credit and Financial Management 78 (October 1976): 33.

32. Agents are classified as (1) direct writers, (2) captive agents and (3) independent insurance agents. Without defining each, suffice to say that agents are state licensed and sponsored by an insurance company. Brokers are also state licensed; however, they are independent of any particular insurance company affiliation. Brokers shop the various companies for the best policy to meet their clients' needs, and generally service commercial accounts.

33. Property insurance, often referred to as the fire policy, generally covers fire, windstorm and hail, smoke and vandalism. Liability insurance generally compensates a third party for an injury, inconvenience or loss he or she has suffered. Liability insurance includes workmen's compensation.

34. "Insurance and Women in North Carolina," Report of the Task Force on Sex Descrimination in Insurance to John Randolph Ingram, Commissioner of Insurance, 1976, p. 27.

35. Ibid.

36. "Federal-State Regulation of the Pricing and Marketing of Insurance," A Report to the Task Force on Antitrust Immunities of the Economic Policy Board, Edited by

Paul W. MacAvoy, (Washington, DC: The American Institute for Public Policy Research, 1977).

37. Insurance regulation was a state matter until 1944 when the Supreme Court held that the sale of property and casualty insurance was inter-state commerce and subject to the provision of federal antitrust laws. (United States v. South-Eastern Underwriters Association, 322 U.S. 533 (1944).) This decision made illegal the private rate-fixing agreements which had determined prices in the property/casualty field, and it raised questions as to the validity of the various types of state regulation of insurance.

The following year Congress enacted the McCarran-Ferguson Act which ratified the states' power to regulate insurance, absent specific federal insurance legislation, and provided an antitrust exemption for private concerted price-fixing activities which were subject to state regulation. The antitrust exemption was justified on the ground that competitive pricing in the insurance field would lead to ruinous competition and the demise of many insurance companies, thereby denying the public the benefit of a reliable insurance mechanism. Thus, all states adopted regulatory schemes relating to property/casualty insurance rates. While some states set the rates themselves, most adopted "prior approval" systems which feature private rate bureaus. Still other states adopted "open competition" systems which allow cartel rate setting but enable insurers to price independently with relative ease.

38. Nancy L. Ross, "Small Business Capital Investment Aid Proposed," Washington Post, 11 February 1978, p. C8.

39. John P. Birkelund, "Capital Gap: A Big Problem for Small Firms," Dun's Review 109 (February 1978): 81-82.

40. Ted Baron, "The Smaller Company's Struggle for Investment Dollars," Public Relations Journal 32 (April 1976): 30-32ff.

41. Birkelund, op. cit.

42. Ross, op. cit.

43. _Dun's Review_ 109 (February 1977): 52-54ff.

44. _Ibid._

45. U.S. Department of Commerce, _Women-Owned Businesses 1972_ (Washington, D.C.: Government Printing Office, 1976). (Hereinafter cited as _Commerce Report_.)

46. Silk, Leonard, "Study for Congress: Slower Growth Ahead," _New York Times_, 9 February 1978.

47. "The State of Small Business, A Report to the President of the United States," Center for Small Business of the Chamber of Commerce of the United States, January 1978.

48. _Report of the SBA Task Force on Venture and Equity Capital for Small Business_, U.S. Small Business Administration, Washington, D.C., January 1977.

49. "Fitting GAAP to Small Businesses," Charles Chagen and Benjamin Benson, _Journal of Accountancy_ LXV (February 1978); 46-51.

50. J. Fred Weston and Eugene P. Brigham. _Managerial Finance_ 5th ed. (Hensdale, Illinois: Dryden Press, 1975), p. 830.

51. SBA, _The Study of Small Business_, p. 3.

52. _Report of the SBA Task Force on Venture and Equity Capital_.

53. _Ibid._, p. 1.

54. _Ibid._, p. 3.

55. Patricia M. Cloherty, Statement Before the Committee on Small Business, United States Senate, January 23, 1978.

56. Margaret J. Gates, "Credit Discrimination Against Women," Vanderbilt Law Review XXVII (April 1974): 410; Barbara J. Klein, "The Equal Credit Opportunity Act Amendments of 1976," Catholic University Law Review XXVI (Fall 1976): 151; Donna Dunkelberber Geck, Equal Credit: You Can Get There From Here -- The Equal Credit Opportunity Act," North Dakota Law Review LII (1975-1976): 382-383; Chesler and Goodman, p. 170.

57. Laurie D. Zelon, "Equal Credit: Promise or Reality?" Harvard Civil Rights-Civil Liberties Law Review XI (1976): 188, 195; Gates, p. 409; Geck p. 388; Maureen Ellen Lally, "Comments: Women and Credit," Duquesne Law Review XII (Summer 1974): 878, 889.

58. Gates, p. 412; Chesler and Goodman, p. 171; National Commission on Consumer Finance, "Hearings and Final Report," 1972; U.S. Congress, Joint Economic Committee, Economic Problems of Women, 93rd Congress, 1st Session, Hearings, July 1973, Part I, pp. 195-202; Dennis Kendig, "Discrimination Against Women in Home Mortgage Financing," Yale Review of Law and Social Action III (Winter 1973): 166-176; "Loans to Women -- A Case For Questioning Lending Criteria," Savings and Loan News, January 1974, pp. 36-42; Jane Roberts Chapman, "Women's Access to Credit," Challenge XVII (January-February 1975): 40-45; Geck, p. 383.

59. JEC, Economic Problems of Women, Hearings, Part I, pp. 202-210, Part III, pp. 572, 587; Eugene Adams, "Bankers Urged to Reconsider Assumptions Regarding Women and Credit," American Banker, June 25, 1973, pp. 12, 22, 26.

60. David H. Swinton, "Factors Affecting the Future Economic Prospects of Minorities," The American Economic Review Papers and Proceedings LXV (May 1975): 53-58.

61. Zelon, pp. 186, 194, 202-205; Gates, p. 412; Geck, pp. 387, 390; Connie Walker Core, "Consumer Protection: The Equal Credit Opportunity Act, Oklahoma Law Review XXVII (Summer 1975): 579; Lily Pilgrim, "A Banker's Primer on Credit Discrimination Against Women," The Banking Law Journal XCIV (April 1977): 349; Kelin, pp. 156-157, 163.

62. June Kronholz, "Women Complain That New Equal Credit Law, Applied Unevenly, Enforced Haphazardly," The Wall Street Journal, 21 January 1977, p. 32+; JEC, Economic Problems of Women, pp. 202, 208-210.

63. Chapman, p. 40.

64. John Charnay, "Women's Banks Not For Women Only," The Bankers's Magazine 160 (Autumn 1977): 103-104, 110; conversation with regulatory agencies.

65. Jenny Tesar, "Anti-discriminatory Women's Banks," Banking, LXIX (October 1977): 66, 72, 77; "Women's Bank: A Special Interest Grows," James Rousemanere, The Baltimore Sun, 11 December 1977, p. K-7.

66. Ibid.; Tesar, pp. 66, 72.

67. "Now a Rush by Women to Start Their Own Banks," U.S. News and World Report, October 27, 1975, p. 62.

68. Tesar, p. 77; Charnay, p.110.

69. "Financial Trouble for Feminists," Time, November 8, 1976, p.99; Charnay, p. 110.

70. Time, November 8, 1976, p. 99; The Baltimore Sun, 11 December 1977, p. K-7.

71. Paula Nelson, The Joy of Money (New York: Bantam Books, 1977), p. 81.

72. U.S. Treasury Department, Internal Revenue Service, Tax Guide for Small Business, 1978 Edition, pp. 1, 3, 150.

73. Literature search for Treasury work for Task Force; Statement of the Honorable Frederic W. Hickman before the Senate Select Committee on Small Business, February 20, 1975, U.S. Treasury Press Release, p. 5; Conversation with Office of Tax Policy, U.S. Treasury Department, February 1978.

74. Ibid.; Hickman, p. 4.

75. Statement of William M. Goldstein before the Senate Select Committee on Small Business and the Subcommittee on Capital Markets, November 13, 1975, U.S. Treasury paper, p. A-3; Coversation with Office of Tax Policy, March 1978.

76. Hickman, pp. 3-4, 6.

77. Task Force Questionnaire.

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79. Small Business Administration, The Study of Small Enterprise in the Economy, Summary, June 1976, p. 6 (hereinafter cited as SBA, Summary); Commerce Report, p. 4.

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121. Tax Guide, pp. 147, 149.

122. Ibid., p. 148.

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124. SBA, The Study of Small Business, pp. iii, 15-21, 30-35.

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126. Ibid.

127. The stock cannot be owned by an estate, trust, or corporation and subsequent owners are not entitled to the advantages of Section 1244. Should small business stock be owned by a partnership, the owner must have been a partner when the stock was issued and remained one until the loss was sustained in order to add his/her distributive share of the loss to his/her individual loss before applying the ceiling on the amount which may be taken as a loss. However, if the partnership distributes the stock to the partner, the stock loss no longer qualifies for ordinary loss but must be taken as a capital loss. Tax Guide, p. 109; House, Ways and Means Committee, Hearings, May 12, 1977, p. 94.

128. The President's 1978 Tax Program: Proposals, IVC-4, pp. 271-272; SBA, The Study of Small Business, p. 19; Lubick, p. 8.

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130. Goldstein, pp. 14-15; SBA, The Study of Small Business, pp. 19, 34, 86,; House, Ways and Means Committee, Hearings, May 12, 1977, p. 94; "Small Business Venture Capital Act of 1977," S. 1815, p. 14.

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132. Tax Guide, p. 126; Richard C. Osborn, "The Supply of Equity Capital by the SBICs," Quarterly Review of Economics and Business 13 (Spring 1973): 69.

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137. The President's 1978 Tax Program, Part I, pp. 2, 13; Fact Sheet 17, pp. 1-2; The President's 1978 Tax Program: Proposals. pp. 19, 28.

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Women business owners are a largely unknown group in the literature. There is little information on women entrepreneurs and women-owned businesses; there is even less on the difficulties women have in obtaining credit and forming a large enough capital base on which to build or expand a small business.

An in-depth search by the Credit and Capital Formation Study Team in the Library of Congress found no books or monographs on the subject. A thorough search was also made in three periodical indices: Public Affairs Information Service (PAIS) (1960-1977), Business Periodical Index (1960-1977), and the Journal of Economic Literature (1972-1977). Many cross references were tried, such as credit, banking, entrepreneurs, loans, small business, and women. In addition, the Federal Reserve Board and all twelve Federal Reserve Banks were contacted and the Center for Women Policy Studies graciously permitted a search of their files. Very few journal articles, monographs, or government publications relating directly and at length to women and commercial loans, bonding, insurance, or venture capital and financing or to articles on taxation and small business were found.

The best sources listed below had little more than a cursory reference to the problems of women business owners in obtaining financing. Many are superficial. The better articles relate to the problems of credit, financing, insurance, etc., of small businesses in general.

Finally, the few excellent articles and other sources on the Equal Credit Opportunity Act presented a thorough analysis of the whole issue of credit discrimination, but they deal primarily with consumer credit.

A word about tangential material is in order. Employment stability and level of earnings are factors in determining credit worthiness. Both the education and socialization of women and the impact of job segregation, due to discrimination and role differentiation on the earnings of women, have a varied and excellent literature. These issues have been well and thoroughly analyzed, but these references have been excluded because they lie outside the specific issues of credit and capital formation.

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APPENDIX

Form Approved: O.M.B. No. 41-S78007

INQUIRY

TASK FORCE ON WOMEN BUSINESS OWNERS

PRIVACY ACT STATEMENT — The Privacy Act of 1974 (P.L. 93-579) requires that you be given certain information in connection with the request for information solicited on this survey questionnaire. Accordingly, pursuant to the requirements of the Act, please be advised that this report is authorized by law; 5 U.S.C. 301, 15 U.S.C. 1512, and 44 U.S.C. 3101. While you are not required to respond, your cooperation is needed to make the results of this survey comprehensive, accurate, and timely. The data will be used solely to provide the input to the Task Force report. There will be no effect on you if you choose not to complete this questionnaire.

Dear Survey Participant:

Thank you for your interest in the work of the Task Force on Women Business Owners which is looking into the problems that potential or existing business owners face.

The Task Force has been charged with the responsibility of collecting information to determine profiles of business owners and their needs, from business owners themselves, people thinking of becoming business owners, and the general public. You are being asked to complete this inquiry because:

- You are a person in business for yourself or are a person considering going into business for yourself, OR
- You have expressed an interest in helping the Task Force on Women Business Owners by adding your opinions and experience to that of many other business owners.

Please answer the following questions as completely as possible. Please feel free to amplify your answers by commenting on any question. Unless otherwise stated, please mark (X) the ONE box which best describes your answer. Since our list of business owners was developed from multiple sources, you may have received more than one copy of this inquiry, if so, please give the duplicate to another business owner or discard it. Please return this questionnaire in the attached envelope within 5 days of receipt, so that your opinions and information can be part of the Task Force's report to the President.

Please return your completed questionnaire to ⟶ Task Force on Women Business Owners 1
P.O. Box 700
Washington, D.C. 20044

1. Did you own a business during any part of 1977?

1 ☐ Yes 2 ☐ No — *SKIP to 18 on page 4*

2. Mark the one statement below that best describes the way you owned this business.

1 ☐ Sole proprietor
2 ☐ Joint or coproprietor
3 ☐ Partner
4 ☐ Own 50% or more of the stock
5 ☐ Own less than 50% of the stock, but am the majority stockholder
6 ☐ Substantial stockholder, but not the majority stockholder
7 ☐ None of these apply — *Describe form of ownership*

____

3. Mark the box which best describes the activity of the business.

1 ☐ Agriculture, forestry, and fishing
2 ☐ Mining
3 ☐ Construction
4 ☐ Manufacturing
5 ☐ Transportation and/or public utilities
6 ☐ Wholesale trade
7 ☐ Retail trade
8 ☐ Finance, insurance, and real estate
9 ☐ Other services — *Specify*

____

4. How many permanent full-time and other employees were employed by this business in March 1977?

	(A) Permanent full-time	(B) Other
None	1 ☐	1 ☐
1–4	2 ☐	2 ☐
5–9	3 ☐	3 ☐
10–19	4 ☐	4 ☐
20–49	5 ☐	5 ☐
50–99	6 ☐	6 ☐
100 or more	7 ☐	7 ☐

5. What were the gross receipts of this business in 1976? In 1977? and what is your best estimate of what the gross receipts will be in 1978?

	(A) 1976	(B) 1977	(C) 1978
Under $10,000	1 ☐	1 ☐	1 ☐
$10,000–$49,999	2 ☐	2 ☐	2 ☐
$50,000–$99,999	3 ☐	3 ☐	3 ☐
$100,000–$499,999	4 ☐	4 ☐	4 ☐
$500,000–$999,999	5 ☐	5 ☐	5 ☐
$1,000,000 or more	6 ☐	6 ☐	6 ☐

6. What percentage of the business is owned by women? ______ %

7. Now, please think of managing (rather than owning) the business. Mark the one statement that best describes your position in this business during most of 1977.

1 ☐ Chief manager or executive officer
2 ☐ Share management responsibilities equally with others
3 ☐ Help manage, but report to someone else
4 ☐ Do not take an active part in the management

8. Now, please think back to the time when you first became an owner of the business.

a. What year did you become the owner? Year ______

b. Were you one of the original founders of that business?

1 ☐ Yes – *Answer c* 2 ☐ No – *Answer d*

c. How did you start that business?

1 ☐ Alone
2 ☐ With spouse
3 ☐ With another family member
4 ☐ With non-family member
5 ☐ With a combination of family and non-family members

d. If you were not an original founder, how did you gain ownership of the business?

1 ☐ Bought the business from a non-family member
2 ☐ Bought the business from a family member
3 ☐ Inherited the business from spouse
4 ☐ Inherited the business from someone else
5 ☐ Gained ownership some other way – *Describe*

______

______

9a. From which of the following sources did you obtain financing and/or capital to become an owner of this business? *Mark ALL that apply*

1 ☐ Personal savings
2 ☐ Joint savings
3 ☐ Family
4 ☐ Friends
5 ☐ Government program
6 ☐ Commercial bank loan
7 ☐ Venture capital firm
8 ☐ Other – *Describe*

______

______

b. How much financing and/or capital did you have from these sources? $ ______.00

10. How would you describe your current relationship with your suppliers?

1 ☐ Very good, have a useful and productive business relationship
2 ☐ Fair, there are some problems but they can usually be worked out
3 ☐ Poor, suppliers cause problems that cannot always be settled
4 ☐ Very poor, suppliers are a major barrier to business success
5 ☐ Not applicable, do not work with suppliers

11a. Have you ever applied for bank credit for the business?

1 ☐ Yes – *Answer b–e* 2 ☐ No – *SKIP to 13*

b. When you first applied for bank credit, how much money were you seeking? $ ______.00

c. How much did you obtain at that time? $ ______.00

d. Was the loan secured?

1 ☐ Yes 2 ☐ No

e. Was the term of the loan for less than one year?

1 ☐ Yes 2 ☐ No

12a. Have you ever applied for bank credit for this business and been turned down?

1 ☐ Yes – *Answer b and c* 2 ☐ No – *SKIP to 13*

b. Did the bank tell you why your application was rejected?

1 ☐ Yes 2 ☐ No

c. What factors do you think influenced the bank to reject your credit application? *Mark ALL that apply*

1 ☐ Lack of collateral
2 ☐ No previous business credit history
3 ☐ Poor business credit history
4 ☐ No previous personal credit
5 ☐ Poor personal credit history
6 ☐ Bank policy regarding small or new business owners
7 ☐ Bank policy regarding female business owners
8 ☐ Bank policy regarding minority business owners
9 ☐ Inadequately prepared loan request
10 ☐ Don't know
11 ☐ Some other reason – *Explain*

______

______

13. Altogether, how many businesses have you owned?

1 ☐ One
2 ☐ Two
3 ☐ Three to four
4 ☐ Five or more

14. Counting all businesses that you have owned, for how many years have you been a business owner?

1 ☐ 1 year or less
2 ☐ 2–5 years
3 ☐ 6–10 years
4 ☐ 11–20 years
5 ☐ 21 years or longer

15a. Have you EVER been the recipient of a Federal Government contract?

1 ☐ Yes – *Answer b, c, and d*
2 ☐ No – *SKIP to 16*

b. From which agency? *Mark ALL that apply*

1 ☐ General Services Administration
2 ☐ Department of Defense
3 ☐ Department of Labor
4 ☐ Department of Health, Education and Welfare
5 ☐ Department of Housing and Urban Development
6 ☐ Other – *Specify*

____

Continue with item 15c

15c. What is the TOTAL dollar amount of Federal contracts you were awarded in 1977?

1 ☐ None
2 ☐ Under $10,000
3 ☐ $10,000–$49,999
4 ☐ $50,000–$99,999
5 ☐ $100,000–$249,999
6 ☐ $250,000–$499,999
7 ☐ $500,000 or more

d. How many Federal Government contracts were you awarded in 1977? Number ______

16. Have you ever been a subcontractor to a prime contractor on a Federal Government contract?

1 ☐ Yes
2 ☐ No

17. The following statements concern PRIME CONTRACTING with the Federal Government. For each statement mark the box which comes closest to your own opinion.

	Agree strongly	Agree somewhat	Neither agree nor disagree	Disagree somewhat	Strongly disagree
a. Most people in my kind of business are familiar with Government contracting procedures.	1 ☐	2 ☐	3 ☐	4 ☐	5 ☐
b. I know where to obtain information about what contracts are available at any given time.	1 ☐	2 ☐	3 ☐	4 ☐	5 ☐
c. I believe it is good business practice to be located in the Washington, D.C. area in order to get Government contracts.	1 ☐	2 ☐	3 ☐	4 ☐	5 ☐
d. The procedures for doing business with the Government are unnecessarily confusing and hard to locate.	1 ☐	2 ☐	3 ☐	4 ☐	5 ☐
e. I know a little more about how to get prime contracts than many other people in my business.	1 ☐	2 ☐	3 ☐	4 ☐	5 ☐
f. There are sufficient opportunities in the private sector, therefore, I do not need to compete in the Government marketplace.	1 ☐	2 ☐	3 ☐	4 ☐	5 ☐
g. I consider myself an able competitor for Government contracts without special programs or assistance.	1 ☐	2 ☐	3 ☐	4 ☐	5 ☐
h. There is a "closed club" of Government contractors that is hard to get into.	1 ☐	2 ☐	3 ☐	4 ☐	5 ☐
i. If I wanted a prime contract, I know how to bid on one.	1 ☐	2 ☐	3 ☐	4 ☐	5 ☐
j. Government contracts are not as desirable as private sector contracts or sales.	1 ☐	2 ☐	3 ☐	4 ☐	5 ☐
k. The Government discriminates against small suppliers when contracts are given out.	1 ☐	2 ☐	3 ☐	4 ☐	5 ☐
l. Female-owned businesses have a somewhat easier time getting contracts than do male-owned firms.	1 ☐	2 ☐	3 ☐	4 ☐	5 ☐
m. Once you get a Government contract, the contracting agency has too much control over the business.	1 ☐	2 ☐	3 ☐	4 ☐	5 ☐

18. The questions below concern agencies or programs that provide information or services to small businesses. Complete these questions even if you were not a business owner in 1977.		Small Business Administration Loan Programs	Small Business Administration Procurement	Small Business Administration Training	Economic Development Administration (Department of Commerce)	Office of Minority Business Enterprise (Department of Commerce)	Other Department of Commerce programs	Farmers Home Administration (Department of Agriculture)	Women's Bureau (Department of Labor)	Health, Education and Welfare Programs	Trade associations	University affiliated programs	Any other? – *Please describe*	
a. Have you ever contacted this agency/program for information or assistance? *(If No, go to next agency/program column.)*	YES	001	002	003	004	005	006	007	008	009	010	011	012	
	NO	013	014	015	016	017	018	019	020	021	022	023	024	
b. How many times have you been in contact with this agency/program in the past 2 years? *(Enter number)*		025	026	027	028	029	030	031	032	033	034	035	036	
c. In general, did you receive the information or assistance you wanted?	YES	037	038	039	040	041	042	043	044	045	046	047	048	
	NO	049	050	051	052	053	054	055	056	057	058	059	060	
d. Mark each of the following services you have received from this agency/program in the past 2 years.														
(1) Loan(s)		061	062	063	064	065	066	067	068	069	070	071	072	
(2) Grant assistance		073	074	075	076	077	078	079	080	081	082	083	084	
(3) Manage or technical assistance		085	086	087	088	089	090	091	092	093	094	095	096	
(4) Counseling		097	098	099	100	101	102	103	104	105	106	107	108	
(5) Printed or prepared information		109	110	111	112	113	114	115	116	117	118	119	120	
(6) Information tailored to your needs		121	122	123	124	125	126	127	128	129	130	131	132	
e. Mark the phrase that best describes how you feel about the **quality** of the information or assistance you received.														
(1) Very satisfied		133	134	135	136	137	138	139	140	141	142	143	144	
(2) Somewhat satisfied		145	146	147	148	149	150	151	152	153	154	155	156	
(3) Neither satisfied nor dissatisfied		157	158	158	160	161	162	163	164	165	166	167	168	
(4) Somewhat dissatisfied		169	170	171	172	173	174	175	176	177	178	179	180	
(5) Very dissatisfied		181	182	183	184	185	186	187	188	189	190	191	192	
f. Mark the phrase that best describes how you feel about the **responsiveness** of the staff in this agency/program.														
(1) Very satisfied		193	194	195	196	197	198	199	200	201	202	203	204	
(2) Somewhat satisfied		205	206	207	208	209	210	211	212	213	214	215	216	
(3) Neither satisfied nor dissatisfied		217	218	219	220	221	222	223	224	225	226	227	228	
(4) Somewhat dissatisfied		229	230	231	232	233	234	235	236	237	238	239	240	
(5) Very dissatisfied		241	242	243	244	245	246	247	248	249	250	251	252	

19. How many years have you worked, including ALL full- or part-time jobs you have held? Exclude work around the house and volunteer work for religious, charitable, and similar organizations.
1 ☐ None
2 ☐ 1 year or less
3 ☐ 2–5 years
4 ☐ 6–10 years
5 ☐ 11–20 years
6 ☐ 21 years or more

20. In total, how many years have you worked in a managerial capacity?
1 ☐ None
2 ☐ 1 year or less
3 ☐ 2–5 years
4 ☐ 6–10 years
5 ☐ 11–20 years
6 ☐ 21 years or more

21. In general, how well have your work experiences prepared you for being a business owner?
1 ☐ Very well
2 ☐ Somewhat
3 ☐ Not at all

22. Mark the one statement that comes closest to your reason for becoming or thinking about becoming a business owner.
1 ☐ I had an idea for a product or service that I thought would sell
2 ☐ I own the business mainly for investment purposes
3 ☐ Owning a business was really just an impulse
4 ☐ I want to make money
5 ☐ I want to take advantage of a particular talent or skill I have
6 ☐ I had to take over the business from someone else
7 ☐ I want to be my own boss
8 ☐ I became a business owner mainly because someone else wanted me to
9 ☐ None of these

23. How many years of formal schooling have you completed?
1 ☐ 0–8 years
2 ☐ 9–11 years
3 ☐ 12 years or high school equivalent
4 ☐ 1–4 years past high school
5 ☐ 5 or more years past high school

24. What types of schools have you attended? *Mark ALL that apply*
1 ☐ Junior or community college
2 ☐ Vocational or technical school
3 ☐ Four-year college or university
4 ☐ Graduate or professional school
5 ☐ None of the above

25. What degrees, if any, do you hold? *Mark ALL that apply*
1 ☐ A.A.
2 ☐ B.A., B.S., or B.F.A.
3 ☐ B.B.A.
4 ☐ M.A., M.S., or M.F.A.
5 ☐ M.B.A.
6 ☐ Ph.D. or D.B.A.
7 ☐ L.L.B. or J.D.
8 ☐ M.D.
9 ☐ Other – *Describe*

____

10 ☐ None

26a. How many semesters of business or math courses did you take in high school?
1 ☐ None
2 ☐ 1–2
3 ☐ 3–5
4 ☐ 6 or more

b. How many semesters of business or math courses have you taken beyond the high school level?
1 ☐ None
2 ☐ 1–2
3 ☐ 3–5
4 ☐ 6 or more

c. If any business or math courses were taken, how useful do you think these courses have been in preparing you for owning your own business?
1 ☐ Very useful
2 ☐ Somewhat useful
3 ☐ Not at all useful

27a. Have you ever talked to a school advisor or counselor about owning your own business?
1 ☐ Yes – *Answer b*
2 ☐ No – *Skip to 28*

b. The counselor's remarks were –
1 ☐ Generally encouraging and supportive
2 ☐ Neutral, neither encouraging nor discouraging
3 ☐ Generally negative and discouraging

28a. Have you ever attended a professional or governmental program or seminar about owning a business?
1 ☐ Yes – *Answer b*
2 ☐ No – *Skip to 29*

b. In general, how useful were they to you?
1 ☐ Very useful
2 ☐ Somewhat useful
3 ☐ Not at all useful

29. Have either of your parents (or guardians) ever owned a business or been engaged in a professional practice?
1 ☐ Yes, father or male guardian only
2 ☐ Yes, mother or female guardian only
3 ☐ Yes, both mother and father (or guardians)
4 ☐ No

30. What is your current marital status?
1 ☐ Never married
2 ☐ Married
3 ☐ Divorced
4 ☐ Separated
5 ☐ Widowed

31. What is your sex?
1 ☐ Female
2 ☐ Male

32. For how many children living in your home do you have or share child care responsibility? | Number

33. How old are you?
1 ☐ Under 25
2 ☐ 25–35
3 ☐ 36–50
4 ☐ 50 or older

34. Mark one box in EACH category.

a. Race
- 1 ☐ American Indian or Alaskan Native
- 2 ☐ Asian or Pacific Islander
- 3 ☐ Black
- 4 ☐ White

b. Ethnicity
- 1 ☐ Hispanic origin
- 2 ☐ Not of Hispanic origin

35. In what State do you now live? State

36a. How many different residences have you had since you were 18 years old? Number

b. How many of these were moves of more than 50 miles? Number

37. Mark the box in column (A) to indicate your household's total income before taxes; then mark the box in column (B) to indicate YOUR contribution before taxes, to the total income of the household.

	Col. (A) Total household income	Col. (B) Your contribution to total household income
Under $5,000	1 ☐	1 ☐
$5,000–$9,999	2 ☐	2 ☐
$10,000–$14,999. . . .	3 ☐	3 ☐
$15,000–$19,999. . . .	4 ☐	4 ☐
$20,000–$29,999. . . .	5 ☐	5 ☐
$30,000–$49,999. . . .	6 ☐	6 ☐
$50,000 or more	7 ☐	7 ☐

Please answer the following questions in your own words. Make your answers as brief or elaborate as you like. Your knowledge and opinions on these issues are very important in shaping the outcome of the Task Force on Women Business Owners. You may attach a separate sheet of paper if necessary.

38. What people and factors influenced you to start your own business?

39. Did your education and work history prepare you for the daily problems in running a business? If not, why not?

40. What information or assistance would be most valuable to you at the point of starting a business?

41. What information or assistance would be most valuable once the business is underway?

42. What recommendations can the Task Force on Women Business Owners make that would benefit you or your business?

THANK YOU FOR YOUR COOPERATION

If you have no objections to your name or business being mentioned in the Task Force report, please mark this box and complete 43 below. → ☐

If this box is blank, your answers WILL REMAIN ANONYMOUS; information will be grouped with other responses and reported ONLY as summaries.

43. The following information is OPTIONAL

Name	Name of business
Number and street	Business address
City, State, ZIP code	City, State, ZIP code

INTERVIEW GUIDE

Name of bank ______________________________

City ______________________________

Person being interviewed ______________________________

Position ______________________ Date ______________________

1. Are your commercial loans broken down into categories for record-keeping purposes?

   1a. If yes, what are the categories?

2. Other than those loans guaranteed by SBA, are small business loans in a separate category?

   2a. If yes, how do you define small business?

   2b. If no, what is the size/range of businesses you make loans to?

3. Do you have a dollar amount cut-off for classfying a loan as being "small business?"

4. Did the general downturn of the economy during 1974 and 1975 affect the proportion of loans your bank could make to small businesses?

5. What has happened since then? Has the amount of money available for small business loans decreased or increased?

6. In view of the current economic forecasts, what do you foresee your policy being toward small business loan assistance in the next two or three years?

7. Does your bank set aside a maximum dollar amount for small business loans each year (or quarter)?

8. What percentage of small business loans are for start-up costs of a new business, i.e., venture capital type loans?

9. Are loans for buying franchises treated differently?

10. What would you estimate the total number of smaller commercial-type loans made per year by your bank to be?

11. Do you know how many of those loans were made to women or firms 50% owned by women active in day-to-day management of the business?

    11a. If no, can you estimate the approximate percentage of loans made to women?

11b. If yes, why do you think more women do not apply?

12. Do you lend in the name of the individual rather than the business entity?

13. Is it often necessary to condition the loan with covenants and/or collateral?

14. Are co-signers usually required?

15. When you are lending to small businesses, are they normally term loans, lines of credit, or transaction lines?

16. How long do you normally go out for term loans to small business?

17. Are any of these loans under Small Business Administration guarantees?

17a. If no, why not?

17b. If yes, how many of the loans are under the guarantees?

17c. If the number is not known, what is the approximate percentage (dollar amount) of total portfolio?

18. How many of the loans under SBA guarantee were made to women?

18a. Percentage?

18b. Dollar amount?

19. Have you found any special difficulties with women applicants under the program?

20. Could you estimate the default rate of SBA loans for us (over any arbitrary time span)?

21. What do you perceive as the primary reasons for default?

22. Does your bank have employees trained in SBA application procedures?

23. Has your bank experienced any difficulties with the SBA loan guarantee program?

24. Has your bank had any involvement with the Economic Development Administration of the Commerce Department?

25. How do customers find you? Do they walk in off the street, or do they come to you by some kind of referral? (e.g., do people call on behalf of someone who needs a loan? Do other bank customers bring in new clients?)

26. Do women come with the same kind of referrals and the same kind of support as men?

27. Do you receive many preliminary phone calls or inquiries from women seeking loan assistance?

27a. If yes, what kinds of questions are usually asked?

28. Has your bank done any research on male versus female pay-back records?

28a. If yes, is there a difference between the two?

29. Could you tell us a little about the people who apply for smaller commercial loans?

Background of applicant: age, education, prior business experience

Is the profile for women applicants different from that of men? If yes, in what way?

30. Are there any common problems with the loan requests you receive?

_____ Inadequate preparation of proposal
_____ Lacking accountant's input
_____ Lacking attorney's input
_____ No market survey
_____ No prior business experience
_____ Bank does not make that kind of loan
_____ Other ______________________
____
____

_____ No projection of expected earnings
_____ No established credit
_____ No money of own to invest
_____ Proposal too high-risk
_____ Company under-capitalized

How much and what kind of experience do you look for?

How much equity and collateral do you look for?

31. Do you have a commercial loan application form?

31a. What kinds of things do you look for in loan applications?

32. If a loan request package is missing something (for example, the market survey is sketchy), what do you do?

33. Do you find you spend much time counseling your small business owners?

34. Do your loan officers get a chance to build a personal knowledge of, or rapport with, the business owners whose loans they handle?

35. Do you keep records on declined smaller commercial loan applications?

35a. If so, how many loans (or percentage) for women were not approved?

35b. If not, can you estimate the proportion?

36. Do a greater proportion of loan requests from women get declined than from men?

37. What are the primary reasons for decline of women's loan requests?

_____ Inadequate preparation of proposal
_____ Lacking accountant's input
_____ Lacking attorney's input
_____ No market survey
_____ No prior business experience
_____ Bank does not make that kind of loan
_____ Other ______________________
____
____

_____ No projection of expected earnings
_____ No established credit
_____ Proposal too high-risk
_____ No money of own to invest
_____ Company under-capitalized
_____ No difference from male applicants

38. When a loan is declined, is the decision made by a single loan officer or by a committee?

39. Does this decision depend on the dollar amount of the loan?

40. What is the make-up of the committee?

41. Is there a review of declined applications?

42. How are loans assigned to portfolios? (e.g., on the basis of type of loan, seniority, geography, etc.)

43. Are the smaller commercial loans usually assigned to specific loan officers?

44. Have you found it useful to assign women loan officers to women applicants, or minorities to minority applicants?

45. How many commercial loan officers are employed by your bank?

46. How many of your commercial loan officers are women?

47. Do you have women in training to become commercial loan officers? How many? Percent of total?

48. Is there an impact on promotions for loan officers if his or her portfolio contains a relatively large number of smaller, higher-risk loans?

49. Are you in a position to know whether your small business clients are receiving the kind of supplier credit they need?

    49a. If yes, are the women owned businesses receiving the supplier support they need?

50. What do you think are the major obstacles to women trying to run a business or start a business?

51. Can you recommend ways more venture capital can be made available to people trying to start new businesses?

52. Approximately how many business depositors do you have?

52a. Of these, how many, or what percentage, are women?

53. Do you recognize women as a viable sector of the entrepreneur market?

54. Does your bank do any special advertising, or conduct programs, to attract women owned business accounts.

55. When the Equal Credit Opportunity Act Regulations include requirements for record keeping for commercial as well as consumer credit, what affect do you envision this will have on your approach to the small business community?

55a. What needs to be rewritten in Regulation B to make operations easier without changing the intent of the law?

Biographical Information

Sex of interviewee__________

Approximate age: 20-29_____

30-39_____

40-49_____

50-60_____

60+ _____

Marital status______________

Number of children__________

Spouse's occupation_________

____

Race____________________

Education Level:

High School____________

Some College___________

B.A., B.S.____________

M.A., M.S., M.B.A._____

Other__________________

Number of years of experience_____________

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